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KOREA

STAFF APPRAISAL REPORT OF

THE MEDIUM INDUSTRY BANK

November 30, 1977

East Asia and Pacific Projects Department
Industrial Development and Finance Division

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CURRENCY EQUIVALENTS

US\$1.00	=	W 485
W 1,000	=	US\$2.06
W 1 million	=	US\$2,061.85

ABBREVIATIONS

ADB	-	Asian Development Bank
BOK	-	Bank of Korea
CGF	-	Credit Guarantee Fund
CNB	-	Citizens National Bank
EPB	-	Economic Planning Board
ERR	-	Economic Rate of Return
ESD	-	Extension Services Department (of MIB)
FLD	-	Foreign Loan Department (of MIB)
FRR	-	Financial Rate of Return
GOK	-	Government of Korea
IFC	-	International Finance Corporation
IRD	-	Industrial Rationalization Fund
KfW	-	Kreditanstalt fur Wiederaufbau
KDB	-	Korea Development Bank
KDFC	-	Korea Development Finance Corporation
KFX	-	Korea Foreign Exchange
KIST	-	Korea Institute of Science and Technology
KFSB	-	Korea Federation of Small Businesses
MIB	-	Medium Industry Bank
NFMIC	-	National Federation of Medium Industry Cooperatives
NACF	-	National Agricultural Cooperative Federation
NIF	-	National Investment Fund
OECF	-	Overseas Economic Cooperation Fund
SIB	-	Small Industry Bureau
SMI	-	Small and Medium Industries
USAID	-	United States Agency for International Development
VAT	-	Value Added Tax

FISCAL YEAR

January 1-December 31

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This report was prepared by Messrs. T.N. Dinh and Alain Soulard following a field appraisal of MIB in August 1977.

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ORGANIZATION CHART

KOREA

MEDIUM INDUSTRY BANK

Basic Data

(As of June 30, 1977)

1. Year of Establishment: 1961

2. Ownership:

	<u>Paid-in Capital</u> (in W Million)	<u>Percent</u>
Government of Korea	13,044	99.9
Private shareholders	16	0.1
Total	<u>13,060</u>	<u>100.0</u>

3. Operations (in W Million)

	<u>1974</u>	<u>1975</u>	<u>1976</u>	<u>1977</u> (6 months)
<u>Approvals</u>				
Domestic currency equipment loans	10,015	7,295	18,755	12,129
Foreign currency loans	9,322	12,369	13,533	10,114
Working capital loans	610,259	843,301	1,174,228	693,616
Total	<u>629,596</u>	<u>862,965</u>	<u>1,206,516</u>	<u>715,859</u>
<u>Commitments</u>				
Domestic currency equipment loans	10,015	7,295	18,755	12,129
Foreign currency loans	9,623	10,109	13,589	4,574
Working capital loans	610,259	843,301	1,174,228	693,616
Total	<u>629,897</u>	<u>862,705</u>	<u>1,206,572</u>	<u>710,319</u>
<u>Disbursements</u>				
Domestic currency equipment loans	9,310	8,000	18,755	12,129
Foreign currency loans	11,726	10,506	13,777	6,393
Working capital loans	609,209	844,351	1,174,228	693,616
Total	<u>630,245</u>	<u>862,857</u>	<u>1,206,760</u>	<u>712,138</u>
<u>Guarantees Issued</u>	<u>11,548</u>	<u>35,899</u>	<u>59,023</u>	<u>32,458</u>

4. Portfolio (W million)

	<u>Equipment loans</u>		<u>Working capital</u>	<u>Guarantees</u>	<u>Total</u>
	<u>Domestic</u>	<u>Foreign</u>	<u>loans</u>		
	<u>currency</u>	<u>currency</u>			
Cumulative commitments through June 30, 1977	83,601	67,805	5,548,495	200,388	5,748,883
Outstanding as of June 30, 1977	36,037	46,256	183,693	4,688	270,674

5. Earnings record

Year ending December 31	<u>1974</u>	<u>1975</u>	<u>1976</u>
	-----percent-----		
Earnings before provisions and tax as % of average total assets	0.4	0.3	0.4
Net income as % of average equity	9.9	7.7	6.3
Financial expenses as % of average total assets	6.7	7.7	8.0
Administrative expenses as % of average total assets	4.0	4.1	3.5
Book value as % of par	214	225	155
Cash dividend as % of par	6	6	-
Dividend payout ratio	29	36	0.2

6. Financial Position (W million)

Total assets	214,430	275,718	342,209
of which loan portfolio	157,831	192,365	234,202
Long-term debt	112,878	131,508	133,266
of which in foreign currency	27,465	35,113	43,619
Equity	6,549	6,882	12,493
Current ratio	1.2	1.2	1.1
Total debt/equity ratio	31.8:1	39.1:1	26.4:1
Long-term debt/equity ratio	15.8:1	17.4:1	9.8:1
Reserves and provisions as % of portfolio	2.2	2.1	2.0

7. Interest Rates and Charges (as of July 1, 1977)

Foreign Currency Loans

IBRD Loan No. 1175-K0	10.5% p.a.
ADB Fourth Loan	10.9% p.a.
Korea Foreign Exchange (KFX)	LIBOR + 2% p.a.

Domestic Currency Loans

Loans for export trade	8% p.a.
Loans to cooperatives	13% p.a.
Government-funded working capital loans	17% p.a.
Government-funded equipment loans	13.5% p.a.
National Investment Fund Loans	13% up to 3 years
	14% from 3 to 8 years
Working capital loans from internal funds	17% for prime borrowers
	18% for other borrowers

	<u>Less than 3 yr</u>	<u>Over 3 yr</u>
Equipment loans from internal funds		
Prime borrowers	16% p.a.	17% p.a.
Other borrowers	17% p.a.	18% p.a.
Discount of trading bills	15% to 19%	
Penalty charge on overdue loans	25% p.a.	

KOREA

MEDIUM INDUSTRY BANK

STAFF APPRAISAL REPORT

1. THE INDUSTRIAL SECTOR

Contribution to the Economy

1.01 Over the past five years, Korea's industrial sector has been growing at nearly 20% p.a. almost twice as fast as the 11% rate of growth of the aggregate GNP. The industrial sector, which accounted for 12% of GNP in 1961, reached 36% in 1976. Manufacturing alone contributed 43% of the increment in GNP over the past decade. Manufactured products represented 90% of commodity exports in 1976, compared with 82% in 1965 and 60% in 1960. Industry has provided about one third of all jobs created since 1963 and as much as 47% over the period 1971-75; with approximately 2.7 million employed, the industrial sector accounted for 20% of the total population employed in 1975 against 11% in 1966. Notwithstanding its impressive contribution to GNP, exports and employment, the industrial sector absorbed only 25.8% of total investment outlays over the period 1972-76, reflecting the efficient use of the economy's scarce capital resources by the industrial sector. In spite of the recent efforts aimed at developing relatively capital-intensive industries such as steel, petrochemicals and shipbuilding, there has been no perceptible increase over the past ten years in the incremental capital-output ratio for the manufacturing sector which remained at 1.3.

1.02 Recent Performance. The Korean economy recovered remarkably well in 1976, after the recessionary period of 1974-75. The performance of the manufacturing sector was particularly impressive with a 26% real growth of value added in 1976,^{/1} second only to the exceptional growth rate of 31% recorded in 1973. Exports increased by more than 40% in volume in 1976, reaching US\$7.8 billion, led by a strong demand for Korea's traditional export products such as textile yarns, fabrics and clothing which maintained a share of about 35% of total commodity exports. Korea's efforts at reducing the concentration of its exports towards the US and Japan have met with considerable success in recent years; in 1976 the combined share of the US and Japan dropped to 56% from a level of 70% in 1974, essentially as a result of the development of new markets in Europe and the Middle East. Commodity exports to the Middle East, earlier negligible, amounted to more than US\$300 million in 1975. In 1976, Korea won construction contracts, mostly in the Middle East, worth about US\$2.5 billion (including the cost of materials and equipment supplied from Korea).

Structure of Industry

1.03 The following table shows the changes in the sectoral composition of the manufacturing sector between the years 1971 and 1975.

^{/1} Compared to 13% in 1975.

VALUE ADDED IN MANUFACTURING /a

	1971		1975		Growth Rate
	Value Added	%	Value Added	%	%
<u>Light Manufactures</u>					
Food, beverages, tobacco	191.0	29.0	268.0	20.4	9
Textiles, footwear, leather,	150.4	22.8	423.6	32.3	29
Wood, furniture, paper printing	48.1	7.3	65.4	5.0	8
Rubber, clay, glass, stone products	40.5	6.1	66.5	5.0	13
Plastics	9.5	1.4	12.1	1.0	6
Subtotal	<u>439.5</u>	<u>66.7</u>	<u>835.6</u>	<u>63.7</u>	<u>17</u>
<u>Heavy Manufactures</u>					
Chemicals, petroleum and coal	117.4	17.8	181.9	13.9	12
Basic metals, metal products	22.3	3.4	51.0	3.9	23
Machinery (including electrical)	35.6	5.4	125.9	9.6	37
Transport equipment	28.1	4.2	81.7	6.2	31
Subtotal	<u>203.4</u>	<u>30.8</u>	<u>440.5</u>	<u>33.6</u>	<u>21</u>
Miscellaneous Industries	16.3	2.5	35.1	2.7	21
<u>TOTAL</u>	<u>659.2</u>	<u>100.0</u>	<u>1,311.2</u>	<u>100.0</u>	<u>19</u>

/a At 1970 constant prices.

Source: National Income in Korea, 1971 and 1975.

Within light manufacturing industries, food processing has declined from 29% of total manufacturing value added in 1971 to 20% in 1975, while textiles, footwear and leather increased from 23% to 32%, due to the sustained demand for these traditional export items. Light manufactures have only marginally declined from 67% of total manufacturing value added in 1971 to 64% in 1975. Conversely heavy manufactures have risen from about 31% to 34% over the same period.

Chemicals, petroleum and coal still make up the single largest subsector within heavy manufactures but the expansion of these industries has been slower than the overall growth of manufacturing value added and their contribution to total manufacturing value added has consequently declined from 18% to 14%. Basic metals and metal products have roughly maintained their share. A substantial increase has taken place in the share of transport from 4% to 6% and more strikingly in the share of machinery which has risen from 5% of manufacturing value added to close to 10%. Machinery manufacturing has had the highest growth rate within the manufacturing sector with an average of 37% p.a. A more radical shift in the structure of the manufacturing sector will be encouraged by the Government in coming years towards more skill-intensive subsectors such as machinery and electronics where Korea enjoys a competitive advantage over other developing countries because of the relative abundance of its skilled labor. This deepening of the Korean industrial structure represents a major objective of the Fourth Five-Year Plan (1977-1981) and is expected to result in a relative reduction in the share of light industries in manufactured exports and output.

Geographic Distribution

1.04 In 1975, approximately 27% of the population of Korea lived in the cities of Seoul and Pusan; the Province of North Gyeongsang where Taegu, the third major industrial city is located, accounted for another 14% of the population. The following table shows that the regional distribution of industry and industrial employment is also skewed in favor of Seoul and Pusan.

GEOGRAPHIC DISTRIBUTION OF INDUSTRY
(%)

	1971			1975		
	No. of establishments	No. of workers	Value added	No. of establishments	No. of workers	Value added
Seoul and Pusan	30.3	45.4	45.2	33.4	45.6	36.5
Other Regions	69.7	54.6	54.8	66.6	54.4	63.5
Total	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>

Source: Report on Mining and Manufacturing Survey, EPB 1975.

There has been little change in the geographic dispersal of industrial employment in Korea between 1971 and 1975; Seoul and Pusan remain by far the largest industrial centers. The Government, however, has become increasingly aware of the need to achieve, through a wider geographic dispersal of

industries, a better distribution of employment opportunities and a reduction of the congestion and overcrowding in Seoul and Pusan. The Government has been promoting the development of industrial centers outside these two areas principally through the establishment of free trade zones and industrial estates. Major examples of this policy are the iron and steel plants in Pohang, the petrochemical complex in Ulsan, the integrated chemical industry in Yeosu, and the machinery center at Changwon. The Saemaeul Movement, initiated in 1971, also aims at creating industrial employment opportunities in rural areas and at reducing the disparities of income between urban and rural areas.

Financial Structure of Enterprises

1.05 The interest rate structure and slowdown in economic activity during the period 1970-72 had resulted in a deterioration of the financial position and structure of Korean enterprises. Companies had become highly dependent on the high cost, short-term "curb market" for their financing. To improve their situation, a Presidential Decree of August 1972 froze all loans from the unorganized money market and new measures were adopted which lengthened maturities of certain loans, reduced interest rates to 16.8% p.a. and converted loans from shareholders into equity. These measures as well as the remarkable performance of the Korean economy in 1973 resulted in a considerable improvement of the financial position and performance of Korean enterprises. The aggregate debt/equity ratio ^{/1} of manufacturing enterprises fell from 3.9:1 in 1971 to 3.1:1 in 1972 and 2.7:1 in 1973. The average interest rate on borrowings of manufacturing enterprises concurrently declined from 13.4% to 8.6%. Profitability improved markedly with net profits increasing from an average of 1% of total assets in 1971 to 7.9% in 1973. With the quadrupling of oil prices at end-1973 and sharp increases in the costs of raw materials, enterprises were again subject to considerable financial strains. Capacity utilization declined and costs of production increased substantially. In an effort to sustain economic activity and employment, the Government helped finance the buildup of manufacturing inventories. Enterprises had to resort to increased borrowings and the aggregate debt/equity ratio increased to 3.2 in 1974 and 3.4 in 1975. Profitability decreased with net income declining as a percentage of total assets from 7.9% in 1973 to 5.7% and 3.9% respectively in 1974 and 1975. Although statistics are not yet available, there is some evidence that with the upturn in economic activity from mid-1975 the financial structure and performance of Korean enterprises have improved.

Industrial Policies

1.06 Over the past ten years, industrial incentives in Korea have been highly responsive to particular and changing circumstances, and varied with Government policies and priorities for industrial development. These policies aimed, with variable emphasis, at the promotion of export industries

^{/1} Source: Financial Statements Analysis for 1975. Bank of Korea.

and of foreign investment, geographic dispersal of industry, assistance to small and medium industries and, more recently, investment in heavy industries.

1.07 A comprehensive incentive system was established during the first half of the 1960s which generally favored exports over import substitution. The main elements of the incentive package included unrestricted access to and tariff exemptions on, imports of raw materials and capital goods, generous waste allowances in determining duty-free raw material imports, direct and indirect tax reductions, access to subsidized credit for working capital and fixed investment, and rate subsidies on certain inputs. Key import substituting industries received protection from imports through tariffs and quantitative import controls. Estimates of effective subsidy rates show, however, that export activity was generally favored over import substitution. The international competitiveness of Korean industry had substantially improved between 1970 and 1973 due to several devaluations of the won, and the Government consequently decided to reduce export incentives. Reductions in corporate income tax were abolished and preferential interest rates increased. In 1975, tariff exemptions on imported inputs were abolished in favor of a system by which the tariff on imported inputs is paid at the time of importation and rebated at the time of export. Tariff exemptions on imports of machinery and equipment by export industries were abolished in 1974, /1 payment of custom duties can, however, be stretched over a three-year period.

1.08 While key import substituting industries have been granted many of the preferences given to exporters, production for domestic sale has generally been subject to higher duties, taxes and interest charges but has benefited from tariffs and restrictions on imports. Over the last few years there has been a modest decline in tariff rates, /2 and increased reliance on import restrictions, /3 as a means of affording protection to domestic producers

/1 Only in the case of capital goods imported under foreign capital financing is there still complete and automatic exemption from tariffs.

/2 The average tariff rate which has remained roughly stable between 22% and 24% in 1969 to 1972 has rapidly declined to about 12.8% in 1975.

/3 The number of prohibited items has declined from 77 in 1968 to 66 in 1975, but items subject to import restrictions have increased from 398 to 579 in 1976.

particularly in the case of capital goods. As a counterpart for the protection afforded to domestic producers through import controls, the Government has established price controls for major commodities./1

1.09 Incentives for the development of domestically manufactured machinery include target ratios of domestically supplied capital goods in the total fixed capital cost for a number of industries and the establishment of specialized medium and long-term government funds to provide won financing for procurement of domestically manufactured machinery. The largest of these funds is the National Investment Fund (NIF) which over the Fourth Five-Year Plan period is expected to finance nearly 18% of investment in the machinery sector and roughly 13% of the total fixed capital formation in manufacturing.

Prospects

1.10 Export orientation has been the dominant feature influencing the structure and rate of expansion of the manufacturing sector. Export growth has been accompanied by a policy of selective import-substitution which has helped the aggregate dependence upon imported intermediate inputs and capital goods remain at roughly the same level over the last decade. Although import substitution has played a significant role in some sectors and over specific time periods, its contribution to the growth of manufacturing output has been very limited. It is estimated that over the period 1960-68 domestic demand contributed some 60% to the growth of manufacturing, while export expansion and import substitution contributed respectively 38% and 2%. The emphasis given to exports of light manufactures has resulted in a rather high degree of dependence upon imports as a source of raw materials and intermediate inputs, as is reflected in the fact that the domestic value added content of Korea's exports is only about 50%. While it is clear that Korea's poor natural resource endowment limits the scope for backward linkages, there is a real need for Korea to undertake a deepening of its industrial structure. Awareness of the desirability of deepening Korea's industrial structure was present in the formulation of both the Second and Third Five-Year Plans and lies behind the decisions to build the first integrated steel mill and petrochemical complex. The long-term plan covering the decade up to 1981 which was published by the Economic Planning Board (EPB) in 1973 emphasized the accelerated development of the heavy and chemical industries as a critical element of Korea's future industrialization. The 1973-74 economic setbacks had rendered a reexamination of this long-term development plan necessary and while, in the Fourth Five-Year Plan, emphasis remains on developing heavy industry and on increasing the domestic content of exported manufactures, some heavy capital and energy-intensive projects have been deferred or cancelled altogether.

/1 In March 1976, Government enacted the Price Stabilization and Fair Trade Law.

1.11 Over the five-year period of the Plan (1977-81), the GNP is expected to grow at a rate of 9.2% p.a. fueled by a 16.5% annual growth in the volume of manufactured exports. The manufacturing sector which now accounts for 32% of GNP is expected to increase at 14.2% p.a., a higher rate of growth than that of GNP, which would bring the contribution of the mining and manufacturing sector to 41% of GNP by 1981. It is expected that some 38% of the two million new jobs to be created during the Fourth Five-Year Plan period will be in the mining and manufacturing sector. As in previous years, Korea's economic development would essentially be export-led, the ratio of commodity exports to GNP which reached 27% in 1975 would rise to 42% by 1981. However, compared to their real growth rate of 32% p.a. over the period of 1967-75, exports are projected to increase at a more modest 16.8% p.a. The Plan is based on the assumption that Korea's exports of textiles, clothing and other light manufactures have a limited growth potential and are subject to encroachment by other developing countries. Korea's comparative advantage will, therefore, increasingly lie in industries which require more skilled labor and greater industrial sophistication such as machinery, electronics and shipbuilding. The real growth of exports of these products would be around 30% p.a. over the 1976-81 period. The share of manufactures is expected to rise from about 85% of total merchandise exports in 1975 to 92% by 1981. In order to sustain the projected GNP growth rate of 9.2% p.a., gross fixed investment would need to rise at 7.8% p.a. In relation to GNP, the projected investment is slightly lower than in the Third Plan period (26.2% of GNP as against 26.9% during the 1972-76 period). The share of manufacturing investment in total gross fixed investment is projected to increase by only 2% from its average share of 24.6% during the Third Five-Year Plan to 26.7% during the Fourth Five-Year Plan. The shift in Korea's export strategy towards more skill-intensive exports is reflected in both the planned structure of industrial output and in projected investment allocations. The share of heavy and chemical industries is expected to rise from 43% of total manufacturing value added in 1975 to nearly 52% by 1981. Investment in light industries is expected to decrease from 40% of total investment outlays in the manufacturing sector over the Third Plan period to 36% over the next five years; conversely, investment in the heavy and chemical industries would increase from 60% to 64%. The share of highly capital-intensive industries such as basic metals, shipbuilding and chemicals would be reduced in relative terms from approximately 75% of investment outlays in heavy and chemical industries over the Third Plan period to 61% over the Fourth Five-Year period in favor of investment in machinery and electronics which would increase from 25% to 39%.

2. THE SMALL AND MEDIUM INDUSTRY SECTOR

Definition

2.01 The official definition of small and medium industries (SMI) in Korea is expressed in terms of employment or assets size and incorporated in the Small Industry Basic Act and the Presidential Decree enforcing the Medium Industry Bank Act which constitutes MIB's charter. This definition was amended on January 18, 1977 to reflect the changes which have taken place in the average size and structure of Korean SMI since 1961, date of the original definition. The following matrix summarizes the new criteria applicable to the various subsectors.

	<u>Total assets</u> <u>(W million)</u>	<u>No. of</u> <u>employees</u>
Mining, manufacturing, transportation	Up to 500	Up to 300
Construction	Up to 500	Up to 50
Commerce and services	Up to 50	Up to 20

Within the SMI sector, there is no official distinction between small and medium enterprises. The official SMI definition governs principally the qualification for membership in the specialized SMI cooperatives (see para 2.14) and the eligibility for domestic currency financial assistance by the Medium Industry Bank. The alternative definition of SMI in terms of either employment or asset size actually leaves open the possibility for some capital-intensive projects to qualify for financing by MIB as long as they meet the employment size limit. This may have happened in the past when the asset limit was fixed at the somewhat unrealistic level of W 50 million (about US\$100,0000). It is expected, however, that with the higher asset limit adopted in 1977 most projects financed by MIB will qualify under both criteria. Based on these new criteria, more than 95% of the loans committed by MIB in 1976 complied with both the employment and asset limits.

2.02 Until January 18, 1977, SMI enterprises in the manufacturing sector (which accounts for about 91% of MIB's portfolio) were defined as those with total assets below W 50 million or with less than 200 employees. Since enterprises which no longer meet the definition of SMI become ineligible for financing by MIB but qualify for financing only by the Korea Development Bank (KDB)/¹ the previous definition resulted in an unduly

¹ At least within the government-owned development banking system since any industrial firm, regardless of size, can approach the privately-owned Korea Development Finance Corporation (KDFC) for financing, although KDFC generally does not finance small industries.

large number of firms, sometimes long-standing clients of MIB, being referred to KDB (as they had grown to exceed both the employees and the assets limits) even though KDB essentially caters to large and sometimes very large industries. It is expected that, with the new SMI definition, previous distortions in the respective operating scopes of MIB and KDB will be alleviated or eliminated. At the same time, MIB, as its scope of operations has expanded, will require access to increased long-term domestic and foreign currency resources.

Role of SMI in the Korean Economy

2.03 In 1975, manufacturing enterprises employing less than 200 persons numbered 21,438 and accounted for 94.1% of the total number of 22,787 enterprises operating in the Korean manufacturing sector. Based on the new (1977) definition of small and medium industries (i.e. manufacturing enterprises employing up to 300 employees), the SMI sector in 1975 employed nearly 650,000 persons (45% of total manufacturing sector employment) and accounted for 96.2% of all manufacturing enterprises, 32% of total value added and 31% of total output but only 20% of total fixed investment by manufacturing enterprises.

Year	<u>No. of enterprises</u>		<u>No. of employees</u>		<u>Value added (in W billion)</u>		<u>Value added per employee (in W '000)</u>	
	SMI	Large	SMI	Large	SMI	Large	SMI	Large
1968	23,555	554	404,906	343,401	107	194	264	565
1972	22,896	833	440,786	532,629	251	648	569	1,217
1975/a	21,438	1,349	534,337	885,807	716	2,112	1,340	2,384
	(21,914)	(873)	(648,955)	(771,189)	(896)	(1,932)	(1,381)	(2,505)

/a Figures in parentheses apply to enterprises employing up to 300 persons.

The above table shows that the relative share of SMI /1 in total employment declined from 54% in 1968 to 38% in 1975. Over the period 1968-1975, the growth of the manufacturing sector has been very rapid: employment increased at an annual average rate of 9.5% and value added in current prices by an average of 38% p.a. The foregoing data suggest that SMI units responded to the expanding demand by increasing employment and moving into the large-scale group of industry. Indeed the average size of employment of Korean SMI units increased by about 6% p.a. over that 7-year period from 17 employees in 1968 to 25 in 1975 while the average size of large enterprises increased only marginally from 620 employees in 1968 to 656 in 1975, a growth rate of less

/1 SMI throughout the following discussion are defined as firms employing up to 200 persons, unless otherwise stated.

than 1% p.a. Another indication of the efficiency of SMI is the fact that labor productivity measured by the ratio of value added per person employed has increased by an annual average of 26% for SMI compared with 23% p.a. for large manufacturing enterprises.

2.04 Exports. While Korean SMI account for just over 30% of total value added and output in the manufacturing sector, their contribution to Korea's exports is considerably greater amounting to US\$2.9 billion or 37% of all commodity exports in 1976. This represents an outstanding performance considering that SMI have maintained their relative share at this level over the last seven years even in 1975 and 1976 when Korea's overall export performance was exceptionally good, and in spite of the rapid expansion of large scale industry in the 1970s. These results show that Korean SMI have been highly responsive to the Government's incentives aiming at an increased export orientation of SMI. Korean SMI are essentially involved in the production of light manufactures, particularly textiles and wearing apparel, which are traditional export items for Korea (textiles and clothing accounted for 36% of Korea's exports in 1975).

Industrial Structure of SMI

2.05 The following table shows the distribution of value added and employment among manufacturing subsectors in the year 1975 for both SMI and large enterprises. In terms of value added, textiles is the most important subsector for SMI with 20.4%, followed closely by food processing (18.4%); chemicals and fabricated metals account both for 17%. In respect of large enterprises (i.e. with more than 200 employees), chemicals comes first with 23.4% followed in order by textiles, food industries and fabricated metals/machinery. These four subsectors account together for about 73% and 84% of the value added generated by SMI and large-scale enterprises respectively. While these figures reflect a great similarity in the sectoral distribution of SMI and large-scale enterprises, larger enterprises are preponderant in the more capital-intensive activities covered under food processing, chemical production, machinery manufacturing and even textiles. Variances in the sectoral distribution of SMI and large-scale enterprises are more pronounced for employment than for value added. This is particularly true for textiles, chemicals and food industries essentially because of the higher productivity of large-scale enterprises in these activities.

STRUCTURE OF THE MANUFACTURING SECTOR IN 1975 /a
(%)

	Value added			Employment		
	Total	SMI	Large	Total	SMI	Large
Food, beverages, tobacco	21.2	18.4	22.1	10.6	12.8	9.1
Textiles, wearing apparel	22.0	20.4	22.7	35.6	30.9	38.4
Wood and wood products	2.6	3.2	2.4	3.7	4.1	3.4
Paper and paper products	3.9	6.8	2.9	4.9	7.9	3.2
Chemicals, rubber, plastics	21.8	17.0	23.4	12.9	10.5	14.3
Nonmetallic mineral products	5.6	11.3	3.6	4.2	5.6	3.4
Basic metals	4.7	3.4	5.2	3.4	3.2	3.5
Fabricated metals, machinery	16.3	17.0	16.0	20.7	20.9	20.7
Other	1.9	2.5	1.7	4.0	4.1	4.0
<u>Total</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>

/a Based on current values and with SMI being defined as enterprises employing up to 200 persons.

Regional Distribution of SMI

2.06 Small and medium-scale industries in Korea are more widely dispersed than large-scale industries. The following table shows that in 1975 only one third of the 22,800 SMI existing in the manufacturing sector were located in the two major industrial centers of Seoul and Pusan. By way of comparison more than 45% of the large-scale manufacturing enterprises were located in these two centers.

REGIONAL DISTRIBUTION OF THE MANUFACTURING INDUSTRY, 1972 AND 1975
(%)

	<u>No. of establishments</u>		<u>No. of workers</u>		<u>Value added</u>	
	1972	1975	1972	1975	1972	1975
<u>SMI</u>						
Seoul and Pusan	30.9	32.6	42.1	40.3	44.9	39.4
Other regions	69.1	67.4	57.9	59.7	55.1	60.6
<u>Large-scale</u>						
Seoul and Pusan	57.3	45.7	56.0	48.7	43.7	35.5
Other regions	42.7	54.3	44.0	51.3	56.3	64.5
<u>Total</u>						
Seoul and Pusan	31.9	33.4	49.7	45.6	44.0	36.5
Other regions	68.1	66.6	50.3	54.4	56.0	63.5

Looking at the regional distribution of employment, it is clear that SMI have been instrumental in creating employment opportunities outside the already congested areas of Seoul and Pusan. Employment in other regions actually increased from 58% of all SMI employment in 1972 to 60% in 1975. Considerable progress has also been achieved by large-scale enterprises from 44% to 51% in other regions but SMI appear to be an effective tool for achieving a balanced geographic dispersal of employment, especially in the less developed areas of Korea. Indications are that SMI located in urban areas tend to be larger, more modern and efficient than their counterparts in other regions.

2.07 To encourage the location of SMI outside the main urban centers, the Government has taken since the early 1970s a number of initiatives such as: (a) the Saemaeul (New Community) movement started in 1971, which promotes the development of small factories in rural areas so as to provide off-farm employment opportunities for rural households /1; (b) the development of Regional Industrial Estates located near secondary urban centers and directed primarily towards the needs of SMI; and (c) Specialized Industrial Estates where industries specialized in a particular activity (e.g. machinery manufacturing) are regrouped and in which larger industries are expected to provide opportunities for subcontracting and the provision of ancillary services by SMI.

Financing of SMI

2.08 Korean SMI receive financial assistance from three sources: (a) the commercial banking system comprising the five nationwide commercial banks and ten local commercial banks; (b) the Citizens National Bank (CNB); and (c) the Medium Industry Bank (MIB). The following table shows the volume of lending by these sources:

LOANS TO SMI BY SOURCE OF FINANCE
(on an outstanding basis in W million)

	1975		1976		June 30, 1977	
	Amount	%	Amount	%	Amount	%
Nationwide banks	341,788	45	437,546	45	530,108	46
Local banks	96,379	13	146,391	15	172,716	15
MIB	183,635	25	225,428	23	255,730	22
CNB	131,396	17	166,498	17	186,378	17
<u>Total</u>	<u>753,198</u>	<u>100</u>	<u>975,863</u>	<u>100</u>	<u>1,144,932</u>	<u>100</u>

/1 By end-1976, a total of 474 Saemaeul projects had been implemented, which were expected to employ close to 50,000 persons and to generate exports aggregating US\$350 million per year.

Over the past three years loans to SMI have averaged about 35% of all bank loans to industry. But most of the SMI financing (about 90% on an outstanding basis) is in the form of short-term working capital loans. Commercial banks do not normally lend long-term funds for equipment financing but have a liberal policy of rolling over short-term lines of credit as they mature. MIB, and to a lesser extent, CNB are the major sources of equipment financing for SMI.

2.09 Commercial Banks. The commercial banks, as shown in the above table, are the major source of finance for SMI. The quasi totality of their financial assistance, however, is in the form of short-term working capital. Commercial banks, including local banks, are statutorily required by the Government to direct at least 30% of their lending to SMI. Compliance with this requirement is supervised by BOK. Loans are granted on the basis of collateral appraisal and of the borrowers' credit standing.

2.10 Citizens National Bank (CNB). The government-owned CNB was established in 1963 to undertake consumers' credit and provide banking services to households and very small enterprises of the cottage industry type. CNB is not authorized to deal in foreign exchange but does provide domestic currency term financing (up to five years) for eligible enterprises i.e. industrial enterprises employing up to 100 persons (until February 1977, the limit stood at 49 employees). Maximum loan size is W 30 million (US\$60,000). (The previous limit until February 1977 was W 5 million). The normal lending rate currently stands at 18% p.a., except for cottage industries which are financed from a special line of credit bearing interest at 8.5% p.a. SMI lending accounted for about 63% of CNB's portfolio which as of June 30, 1977, stood at W 293 billion. The balance consisted of personal loans whose term is usually less than three years. CNB derives its financial resources mainly from deposits and from borrowings from the Government and BOK. At end-June 1977, its total assets amounted to W 478 billion and its staff numbered about 5,000 persons most of whom were employed in the 132 branches and offices scattered around the country. CNB lends on the basis of collateral and does not undertake project appraisal.

2.11 Fixed Investment in SMI. Total fixed assets investment by manufacturing industries reached W 838 billion in 1975; enterprises employing up to 200 employees accounted for about 16% of that total with W 130 billion (about US\$270 million). MIB estimates that about 66% of all SMI fixed investment in 1975 was in machinery and equipment while buildings and land accounted for 26% and 8% respectively. Studies by MIB have shown that SMI fixed investment is financed up to 60% by the companies' own funds and the balance from borrowings. Loans from institutional sources (e.g. commercial banks, MIB, CNB) accounted for only approximately 60% of SMI borrowings, suggesting that SMI enterprises had to rely to some extent on private borrowings, including those from the curb market. However, the fact that over the past three years loans to SMI had accounted for 35% of all bank loans to industry (para. 2.08), compared with SMI's share of 30% of total industrial output, indicates that SMI units have had relatively easy access to bank credits.

Nonfinancial Assistance to SMI

2.12 Government Policy for SMI. The Government's program of promotion of SMI was initiated in the early 1960s with the establishment of the Small Industry Division in the Ministry of Commerce and Industry and of the Medium Industry Bank in 1961. At first Government's efforts were largely confined to channeling financial assistance and ensuring that adequate technical assistance was available through MIB's extension services. Recognizing the role of SMI in generating employment outside the main urban areas, in contributing to the growth of exports and in complementing large industries through subcontracting and the provision of ancillary services, the Government introduced additional specific policy measures and incentives in favor of SMI. These measures include: (a) the 1971 Saemaeul Program, under which loans are provided at preferential interest rates, along with easy access to industrial utilities, land and concessionary tax rates for SMI establishing in rural areas; (b) incentives given to export-oriented SMI to relocate in industrial estates and export zones and to create groups of exporting SMI for the marketing of their production overseas; (c) special depreciation allowances encouraging modernization of machinery and productivity improvements; and (d) promotion of mergers. As for SMI at the smaller end of the spectrum whose access to bank financing is hampered by the lack of collateral, the Government has progressively strengthened the Credit Guarantee Fund which issues guarantees to small industrial borrowers. Previously administered by MIB, the Fund has been operating independently since 1976.

2.13 Small Industry Bureau (SIB). Originally a division of the Ministry of Commerce and Industry, the SIB is responsible for the formulation and implementation of government policies for SMI. The SIB monitors progress in the SMI sector and gathers information on SMI. Due to its small staff, the SIB relies heavily on MIB, the National Federation of Medium Industry Cooperatives and the provincial governments to carry out its functions.

2.14 Korea Federation of Small Businesses (KFSB) /1. Established in 1962 under the Small and Medium Industry Cooperatives Act, the KFSB is the apex institution of SMI cooperatives throughout the country. The small business cooperative structure comprises 64 federations at the national level and 109 cooperatives at the provincial level. These cooperatives perform a number of functions for their members including provision of managerial and technical guidance, dissemination of economic and business information, joint purchase of raw materials, marketing assistance, etc. The cooperatives' operations are partially funded by the Government either through direct grants or indirectly through tax exemptions and subsidized loans.

/1 Previously named the National Federation of Medium Industry Cooperatives (NFMIC).

Reexamination of SMI Policies and Institutional Framework

2.15 In spite of the considerable success of the SMI sector in the past, the Government is in the process of undertaking a comprehensive review of its policies and institutional framework, with a view to further strengthening it and enhancing the Government's assistance to it. Measures being contemplated by responsible Government officials include the following:

- (a) an overhauling of the administrative machinery involved in SMI. An "Office of SMI" is expected to be established, which would act as the central authority in all SMI matters. This office (to be headed by a Government official with the rank of a Vice-Minister), would be essentially an offshoot of the existing Small Industry Bureau (para. 2.13), which it would absorb, but considerably strengthened in terms of statutory powers and staff;
- (b) a strengthening and possible reorganization of the Korea Federation of Small Businesses and of the system of SMI cooperatives referred to in para. 2.14;
- (c) greater financial assistance to SMI by the Government including increased access by MIB to government resources (e.g. budgetary allocations and borrowings from the National Investment Fund);
- (d) a reexamination of the existing system for delivery of extension services to SMI enterprises (which at present relies essentially on the Extension Services Department of MIB) with a view particularly to facilitating the transfer of appropriate technologies;
- (e) mergers of SMI enterprises to achieve economies of scale; and
- (f) a general review of the overall incentives system concerning SMI.

3. THE FINANCIAL SECTOR

Institutional Setup

3.01 The financial sector of Korea consists of the Bank of Korea, Deposit Money Banks and nonmonetary financial institutions. The Bank of Korea performs regular central banking functions, including the supervision of commercial banks.

3.02 Deposit Money Banks include commercial banks and specialized banks. Commercial banks receive most of their funds through deposits from the public. They can make all kinds of loans but have traditionally concentrated on short-term lending although term financing through roll-over of short-term loans is common. There are 5 nationwide commercial banks, 10 banks with localized operations and 11 branches of foreign banks which together had 693 branches/offices around the country at end-1976 (all these fall into the category of "commercial banks"). Four of the five nationwide commercial banks are

are fully controlled by the Government which, under Korean law, automatically receives majority rights if its holding in a nationwide bank is 10% or more. The fifth bank is controlled by the semiofficial Korean Traders Association. All commercial banks are subject to control and supervision by the Bank of Korea while specialized banks are directly controlled by the Ministry of Finance. The specialized banks were all established under a Special Banking Act and are subject to only a few specific Articles of the Bank of Korea Act and General Banking Act. Specialized banks are government-controlled and/or owned. As their name implies, they were founded for particular purposes or sectors (such as small-scale industry financing or agricultural financing) and government funds constitute a substantial part of their financial resources in addition to resources raised otherwise, the bulk of which consists of deposits raised from the public, hence their categorization as Deposit Money Banks. Specialized Banks include the Korea Exchange Bank, which was established in 1967 mainly to relieve the Bank of Korea of commercial foreign exchange business, the Medium Industry Bank which extends financial and technical assistance to small and medium-scale industries, the Citizens National Bank (mainly for mobilizing small savings and financing household loans and small enterprises), the Korea Housing Bank, the National Agricultural Cooperative Federation (NACF) and the National Fisheries Cooperative.

3.03 Besides the above-mentioned banking institutions which, with the BOK as supervising agency, constitute the "Monetary System," there are several nonbanking financial institutions, namely: (a) development finance institutions; (b) savings institutions; (c) life insurance companies; and (d) investment companies. The development finance institutions comprise the Korea Development Bank (KDB) which so far has received two Bank loans totaling US\$142.5 million,^{/1} Korea Development Finance Corporation (KDFC) to which Bank Group assistance, including IFC, amounts to US\$240 million to date,^{/2} the Land Bank and the Export-Import Bank. Savings institutions comprise some 1,200 authorized credit unions (at end-1976) and 211 mutual savings and finance companies. Five life insurance companies operate in Korea, in addition to the postal life insurance and the Educational Insurance Company. Investment companies include the Korea Securities Finance Corporation which is the principal organization for securities financing in Korea, the Korea Investment Corporation, primarily an underwriter and broker of corporate securities, the newly established Korea Merchant Banking Corporation, ten short-term finance companies^{/3} and the Korea Investment Trust Corporation which is specialized in the establishment of investment trust funds. In addition, three leasing companies have been established over the last few years as joint ventures between Korean and foreign investors.

^{/1} Please refer to report No. 1255-KO dated September 30, 1976: Appraisal of Korea Development Bank.

^{/2} Please refer to report No. 1578-KO dated May 26, 1977: Appraisal of the Korea Development Finance Corporation.

^{/3} Including the Korea Investment Finance Corporation (KIFC).

3.04 As of December 31, 1976, total loans outstanding to the manufacturing sector by all banking institutions in Korea including KDB amounted to W 2,437 billion (US\$5.0 billion equivalent). About 70% of this amount was for operating funds, mainly supplied by commercial banks. The largest supplier of equipment fund loans is KDB which, as of December 31, 1976, had an outstanding term portfolio of W 226 billion (US\$466 million), about 45% of the total outstanding medium and long-term credit by banking institutions to industry as of that date.

Capital Market

3.05 The Korea Stock Market was moribund for many years but showed signs of life in 1972. Before then the yields on stocks were considered unattractive as both savings accounts of commercial banks and the "curb market" gave higher returns. The market was also thin because closely held companies were reluctant to go public. With the mid-1972 economic boom and the adoption of new financial measures by the Government (para. 1.05), the public showed growing interest in the stock market. The curb market was severely checked as a result of the August 1972 measures and with decreasing interest rates served by commercial banks, yields on stocks became attractive. In addition, the overall investment climate became more favorable after August 1972, and the campaign for more stock listings and for companies to go public was intensified. The result was a large increase in stock exchange activity in the second half of 1972 and in 1973. In 1974, however, trading activities on the exchange slowed down considerably, due to the gloomy business outlook; new stock listings, however, continued to rise reaching almost W 500 million at the end of 1974. The following table summarizes the stock exchange activity over the last six years (figures are shown as of the end of each period):

STOCK ACTIVITY 1971 - 1976

	No. of listed companies	No. of shareholders (in '000)	Capital of listed stock (W billion)	Market value of listed stock (W billion)
1971	50	81.9	141.4	108.7
1972	66	103.3	174.3	246.0
1973	104	200.0	251.6	426.2
1974	128	199.9	381.3	532.8
1975	189	290.7	643.4	916.0
1976	274	764.9	1,153.3	1,436.1

3.06 With the general improvement of the business climate and improved export prospects, trading picked up again around mid-1975 and for the year as a whole the number of stocks listed almost doubled.

3.07 In 1976, the capital market was rather sluggish in comparison to the previous year mainly because of the Government's tight monetary policy.

The general stock price index stood at 415.3 at end-1976, an increase of 8% only during the year, compared with a 44% gain a year earlier. On the other hand, the issuing market was very active during the year as a result of the Government's efforts to promote the "going public" of privately held companies. The number of listed companies increased by 85 to 274 in the year and a total of W 263 billion was mobilized through the capital market, a 69.5% gain over the previous year. During the year, the number of shareholders increased substantially. Over the years, the ownership structure has broadened, though as at October 31, 1976, more than 68% of all shareholders still held less than 100 shares each and accounted for only 2.05% of all shares outstanding. The importance of the Government as a shareholder of listed companies also decreased; while the Government (including public bodies) held about 39% of the total number of listed stocks in 1970, its holdings had declined to 13% by October 31, 1976. The proportion held by banking institutions also declined from 15% to 9% during the same period.

3.08 The rapid increase in the volume of operations on the Stock Exchange had rendered certain improvements necessary. Among others the call market has been replaced by a continuous auction market, investment trust companies have been established, and the information system greatly improved. Several weaknesses remain, however. One of the more important problems lies in existing laws which stipulate that new equity issues have to be at par irrespective of the market price of stocks. These regulations are currently under review by the Government.

Interest Rates

3.09 The Government through the Monetary Board determines interest rate ceilings on deposits and loans which apply to all banking institutions. Although private specialized financial institutions such as KDFC or the short-term finance companies are not legally bound, in practice, they too have to follow government policies. The development of Korea's interest rate structure has, between 1968 and 1973, seen a continuous reduction in both deposit and lending rates. The lowering of the rates coincided with the Government's success in gradually bringing inflation down until late 1973. With the emergence of the oil crisis and worldwide inflation, Korea's price structure was particularly hard hit because of its high foreign trade dependence. Wholesale prices are estimated to have increased by nearly 80% between the end of 1973 and the end of 1975. While the Government selectively increased interest rates at the end of 1974, /1 a general increase of interest rates was postponed because enterprises were already facing severe financial strains and the Government hoped to succeed in bringing inflation under control. During the year 1976, wholesale prices are estimated to have increased by 12.1% on an annual basis.

/1 Raising rates on time deposits for over three months and over six months from respectively 12% and 13.2% to 15%, and preferential rates for loans from the NIF and IRF from 9% and 8% respectively to 12%.

3.10 On August 2, 1976, the Government made an extensive upward adjustment in the interest rate structure in order to contain excessive loan demand and to better allocate funds. To stimulate domestic savings, the interest rates on time deposits were raised by 1.2% to a level of 16.2% p.a. for long-term deposits and by 2.1% to the level of 15% p.a. for short-term savings deposits. "General lending rates" /1 have correspondingly been increased by 1.5% to 3.5% and now range between 17% and 19% p.a. depending on (a) the credit standing of the borrower for working capital loans (with a differential of 1% in the applicable rate); and (b) loan maturity for equipment financing (with rates of 17% p.a. for loans maturing in less than three years, 18% for three to eight years and 19% over eight years). Preferential interest rates applicable to loans from specialized government funds such as NIF and IRF also differentiate according to maturity and have been increased from 12% to 13% for three-year loans and 14% for those in excess of three years.

3.11 Prior to August 1976, Korean commercial banks had already resorted to various practices which resulted in increased collateral requirements and higher effective lending rates for their less creditworthy borrowers. Such practices include the collection of interest in advance, /2 the establishment of compensating balances on time deposits or even the opening of installment saving accounts which are used both as collateral and sinking funds. Actual requirements vary among borrowers depending on their credit standing. The August 1976 measures can, therefore, be construed as ratifying and rationalizing a system which already differentiated between borrowers on the basis of the risks involved. The Korean financial authorities now have established a list of criteria for enterprises to qualify as prime borrower which should eliminate subjective judgments on a company's creditworthiness. The introduction of a prime rate system for working capital loans and of differential rates according to loan maturities constitutes an important step towards improving the overall allocation of funds to industry.

3.12 Effective July 1, 1977, the Government replaced the previous excise, business and consumption taxes by the value added tax (VAT) system, all goods and services being assessed at a flat rate of 10%. There is some apprehension amongst the general public and business community that the new taxation system might result in an increased tax burden on industrial enterprises and consequently in sharp rises in the cost of living. While the Government did not subscribe to this thinking, it had decided to moderate the

/1 Unless otherwise specified, this discussion applies to the so-called "general lending rates" as opposed to the "preferential rates" applicable to various priority sectors. Generally speaking, general lending rates are applicable to loans made by KDB, MIB and Deposit Money Banks from their own funds (essentially deposits and equity); preferential rates apply to loans made from specialized government funds (NIF, IRF, etc.). At end-1976, loans at preferential interest rates accounted for approximately 40% of the total outstanding portfolio of banking institutions in Korea.

/2 Quarterly or monthly depending on the financial rating of the borrower.

possible adverse impacts of the new tax system by introducing various anti-inflation measures including a lowering of the banks' lending rates by 1% effective July 1, and by another 1% October 1, 1977. Time deposit rates have also been lowered by 1.8% from October 1, 1977. While Korea maintained positive real interest rates from 1965 through 1973, inflation as measured by the Wholesale Price Index reached 42% and 26% in 1974 and 1975 respectively, thus resulting in substantially negative interest rates in real terms. Inflation was sharply reduced to just over 12% p.a. in 1976 and is expected to remain at the same level in 1977, in excess of the Fourth Five-Year Plan target of 7% p.a. Even assuming that inflation slightly exceeds the Plan target in coming years, the overall decline in the interest rate structure mentioned above should leave real interest rates at a positive level.

4. THE MEDIUM INDUSTRY BANK /1

A. Legal Framework, Organization, Policies and Procedures

Legal Framework and Ownership

4.01 Until 1961 loans to small enterprises in Korea were handled by commercial banks and the government-owned Korea Agricultural Bank as an addition to its normal agricultural credit activities. The Medium Industry Bank (MIB) Act of July 1, 1961 provided for the establishment of a new financial institution specializing in extending financial and technical assistance in various forms to small and medium-scale industries (SMI), as defined in the Presidential Decree of August 1, 1961 enforcing the MIB Act. As a specialized financial institution, MIB's operations are governed by the provisions of the MIB Act and are subject to the broad supervision of the Ministry of Finance. The Articles of the General Banking Act which govern the operations of commercial banks apply also to MIB's commercial banking activities, e.g. mobilization of deposits, discounting of bills, letters of credit; these activities are further subject to the supervision of the Bank of Korea. The Act constitutes MIB's charter and establishes the broad framework for its policies, scope of activities, administration and capitalization. The Act also specifies the scope of the supervision to be exercised by the Minister of Finance whose approval is required for the adoption and/or revision of MIB's by-laws, operating manuals, annual plan of operations, appropriation of earnings and the appointment of MIB's top management.

4.02 Although the MIB Act stipulates that government ownership of MIB's share capital shall be 50% or more with the balance to be held by small and medium entrepreneurs, private shareholders held only 0.1% of MIB's share capital as of June 30, 1977. These private holdings, amounting to W 16 million, actually resulted from arrangements made for the disposition of excess dividends following the liquidation of the Federation of Financial Associations of Korea at the time of MIB's establishment. The MIB Act was last amended in December 1975, essentially to accommodate an increase of W 24 billion (from W 6 billion to W 30 billion) in MIB's authorized share capital. At end-June 1977, MIB's paid-in share capital stood at W 13.1 billion, a W 10 billion

/1 The English name of "Medium Industry Bank" was the result of an original translation mistake. The official name of the institution in Korean is "Small and Medium Industry Bank."

increase over the December 1975 level. This increase resulted from cash subscriptions to MIB's share capital by the Government in accordance with an agreement reached during negotiations of the first IBRD loan in 1975. The Government at that time undertook to further increase MIB's share capital as needed in the future, so as to maintain its long-term debt/equity ratio within the agreed limit of 10:1.

Organization and Operational Autonomy

4.03 The MIB Act provides for a dual Board setup. The Board of Policy, which deals with broad policy matters, comprises seven members including MIB's President who acts as its Chairman, one representative each from the Ministry of Finance, the Ministry of Commerce and Industry, the Bank of Korea, the National Federation of Small and Medium Industry Cooperatives and two representatives of small entrepreneurs (the latter two being selected by the Minister of Finance). The Board of Policy convenes on an average of three times a year, primarily to approve the settlement of MIB's annual accounts and the appropriation of earnings, any amendments to the by-laws and operating manuals, and MIB's annual plan of operations. Resolutions of the Board of Policy regarding the above matters are subject to the approval of the Minister of Finance.

4.04 Executive authority, including the approval of loans and guarantees exceeding certain ceilings, is vested in the Board of Directors. The latter is composed of seven members, including MIB's President, acting as Chairman, the Deputy President and the five Directors in charge of MIB's various departments. The dual Board setup and the demarcation of functions between the two Boards, as described above, have proved to be appropriate and effective. On the one hand, it enables key government officials and representatives of the SMI business community to participate in broad policy deliberations within the Board of Policy, thus facilitating the flow and exchange of information between MIB, the Government and the private sector. On the other hand, it concentrates executive authority in the Board of Directors, which, in effect, is a full-time professional body comprising MIB's senior management team. With this dual Board setup, MIB operates within the ambit of government policies while enjoying full autonomy in its operational decisions. The composition of the two Boards is given in Annexes 1 and 2.

Management

4.05 Mr. Nam Sang Jin, a former Vice-Minister of the Ministry of Finance, was appointed as MIB's President and chief executive officer in May 1976. He has extensive experience in banking and financial matters. He is assisted by a Deputy President (formerly an Assistant Governor of the Bank of Korea) and five directors, all of whom have had long experience with MIB and its predecessor, the Korea Agricultural Bank. Each Director is in charge of 3 to 4 of MIB's 17 departments (see Organization Chart). Historically, MIB's Presidents have been appointed from the senior levels of the government hierarchy. Although there has been a rapid turnover of Presidents in the last four years (Mr. Nam is the third President within that time span), management continuity has been maintained through the Directors and Department Managers. MIB has an experienced and competent cadre of managers in its departments and branch offices. It also has considerable depth at the deputy manager level.

Staff

4.06 The mobilization of demand and savings deposits, which represents a major source of funds for MIB's operations, requires a nationwide network of 65 branches and 13 smaller deposit offices. As a result, the size of MIB's staff as well as the level of its administrative expenses are more comparable to those of commercial banks than to conventional DFCs with which the Bank is associated. Of its total staff of 3,533 as of June 30, 1973, only 23% were employed at the head office with the remaining 77% in MIB's branches and deposit offices. Under MIB's own classification all employees with a college degree are considered as professionals; some 84% of its total staff would qualify as such. This percentage includes, however, a large number of personnel performing clerical, banking (e.g. tellers) and administrative functions typically categorized as subprofessional. Excluding those, the proportion of professionals to total staff is about 25%. MIB recruits mainly college graduates who undergo throughout their professional career comprehensive on and off-the-job training and whose rotational assignments are planned so as to develop versatility. While this policy may sometimes cause a certain disruption in the activities of the departments affected, it has also enabled MIB to build up a solid cadre of experienced and well-rounded professionals at the middle management level. Staff training at the various levels is comprehensive and methodical. The overall quality of MIB's staff is good.

4.07 The growth of MIB's staff has averaged 4% p.a. over the past five years, which has been sufficient for MIB to cope with the growing volume of its business. MIB's departments appear to be adequately staffed including the Foreign Loan Department (FLD), which is responsible for processing loan applications in foreign currency, and the Extension Services Department (ESD), which provides technical assistance. A strengthening of the staff of these two departments was urged by the Bank and agreed to by MIB at the time of negotiations of the previous Bank loan. This undertaking has been satisfactorily implemented, but a further and gradual strengthening of the FLD may prove necessary as its volume of business increases.

4.08 Staff turnover at the professional level, which was very moderate through the first half of 1975, increased rapidly thereafter and is likely to exceed 10% in 1977 as it did in 1976. This is attributable to a gradual erosion, in relative terms, of compensation in the government banking sector vis-a-vis the industrial private sector. Turnover is particularly heavy at the middle-management level and for staff with a working knowledge of English. The Government, which determines the level of salaries in government banks, recently acceded to the request of the management of these banks for a sizeable salary increase which should come into effect around the end of 1977. While the recent staff turnover has had no discernible adverse impact on MIB's operational efficiency, MIB's management is keeping the situation under close review and is prepared to intensify recruitment of suitable additional staff.

Operating Policies and Development Strategy

4.09 In conjunction with the securing of the first ADB loan in 1969, MIB's Board of Policy adopted a Policy Statement which supplements the broad

policy and operational guidelines contained in the MIB Act (Annex 20). Aside from restrictions on the maximum exposure which MIB is normally authorized to take in any single enterprise, this statement defines in broad terms the industries which are to be given priority for MIB's assistance (essentially export-oriented and import-substituting industries as well as labor-intensive projects). The financial guidelines do not specify any statutory limit on MIB's long-term debt/equity ratio. A contractual limit of 10:1 has, however, been agreed to by MIB with IBRD and ADB. MIB's debt/equity ratio stood at 7.4:1 as of June 30, 1977.

4.10 In order to emphasize its immediate developmental objectives, MIB formulated in 1975 a Development Strategy covering the period 1976-77 which outlined the following areas on which it intended to focus:

(a) a greater geographical dispersal of portfolio outside the main industrialized areas of Seoul and Pusan; (b) intensified assistance to Saemaeul rural industries; (c) intensification of its extension services; and (d) increased mobilization of long-term domestic currency resources. MIB has made substantial progress in implementing these objectives and intends to continue to give them high priority in the next two-year period. MIB has consequently updated its strategy statement with renewed emphasis being placed on geographic dispersal, rural industries, development of small, labor-intensive projects and the provision of extension services to SMI (Annex 21).

Project Appraisal

4.11 For short-term working capital loans, MIB's lending decisions are essentially based on an assessment of the borrowers' credit standing and of the collaterals available rather than on project analysis, a practice in line with commercial banking. MIB's appraisal work for term loans is sound. Technical analysis in MIB's appraisal reports is generally quite thorough and benefits from the assistance received from the engineers of the Extension Services Department and, since April 1977, from the Korea Institute of Science and Technology (KIST) for technical matters in which MIB's engineering staff does not possess sufficient expertise. Technical feasibility as well as the borrower's credit standing are given foremost consideration by MIB, which is an appropriate approach for small business lending. The quality of market analysis often suffers from the lack of information on small and specialized markets relating to SMI projects, but the widespread practice of subcontracting for Korean SMI limits the marketing uncertainties. Financial and economic analysis has gradually been expanded and improved by MIB in connection with the submission of some 140 subprojects under this first Bank loan. Sensitivity analysis has recently been introduced using different price and cost assumptions, and partial economic indicators (i.e. employment, value added and balance of payments impact) are routinely calculated. The calculation of economic rates of return was recently undertaken for a few projects requiring MIB's financing in excess of \$0.5 million. Although there is room for further upgrading various aspects of MIB's appraisal, the desirability of a more refined appraisal work (which would necessarily be more time-consuming) ought to be weighed against the desirability of accelerating loan processing, especially for a small industry lending institution such

as MIB. MIB takes the reasonable view that its appraisal work at present is basically satisfactory and that it is more important to speed it up than to attempt to further refine it. During appraisal, MIB agreed that: (a) with a view to speeding up loan processing by MIB, substantially simplified criteria and procedures will be applied under the proposed loan by MIB to free-limit subloans. Instead of a full appraisal report, MIB will submit to the Bank a simplified "Project Summary" giving the essential financial and economic project data for these subloans; and (b) the calculation of economic rates of return will be made for projects requiring subloans exceeding US\$500,000, with, however, the exception of expansion projects (i.e. for additional capacity), for which the economic rates of return are usually less meaningful, and of export-oriented projects, for which a reasonable financial rate of return would in most cases suggest economic viability as well.

Project Follow-up

4.12 Follow-up work is delegated entirely to the branch offices, except for foreign currency loans, the supervision of which is the responsibility of both the Foreign Loan Department at headquarters and of the branches. Loan agreements with subborrowers give MIB the right to inspect, as need be, the premises of the projects and specify reporting requirements which include the periodic submission of financial statements, information on production, sales and changes in management or production facilities. Field visits are normally conducted at least twice a year and more frequently for problem projects. Because most term borrowers also receive working capital loans and maintain both current and time deposit accounts with MIB, branches have frequent contacts with clients and an early knowledge of the liquidity situation and of any financial difficulties which borrowers may face. Recognizing this special position of its officers in the branches, MIB recently started training the branch deputy managers in simple managerial and technical diagnosis with a view to improving consultancy services at the branch level. (More complex problems are referred to the Extension Services Department at the head office.) Referral of problem projects to the Loan Settlement Department (LSD) takes place when a loan officer recommends that the loan be rescheduled or that legal proceedings be undertaken to foreclose the account. Write-offs, too, are subject to scrutiny by the LSD and approval by the Loan Settlement Committee.^{/1} The effectiveness of MIB's follow-up work is reflected in the quality of its portfolio and the low level of arrears.

4.13 Following discussions with the Bank at the time of negotiation of Loan 1175-K0, MIB introduced a Project Monitoring System for a sample of 50 subprojects appraised by the Foreign Loan Department. The objective of the system was to evaluate progress at critical stages of implementation of the projects and to analyse actual project costs and benefits for comparison with earlier appraisal estimates. In spite of the substantial staff time required to carry out such a system, MIB appreciates its benefits and intends to gradually expand it.

^{/1} Which is composed of the Deputy President, the five directors and the managers of the LSD and Auditing Office.

Procurement and Disbursement

4.14 MIB's procurement and disbursement procedures are laid out in detail in its Operating Manuals and duly enforced. Procurement procedures for foreign currency loans are tailored to meet the requirements of each line of credit. The technical staff of the Extension Services Department helps MIB's borrowers draft invitations for bids and supervises the opening of bids. Procurement is normally based on at least three competitive quotations from foreign suppliers and the final contract is subject to MIB's approval. Under domestic currency term loans, funds are deposited into a special account in the borrower's name and released according to the progress made in implementing the project as certified by the loan officer. MIB's procurement and disbursement procedures are satisfactorily designed to ensure the efficient and appropriate use of funds.

B. Operations and Developmental Impact

Scope of Operations

4.15 Within Korea's institutional framework for industrial financing, MIB occupies a median position between, at one end, the government-owned Korea Development Bank (KDB) and the privately-owned Korea Development Finance Corporation (KDFC) which both concentrate on relatively large enterprises and, at the other extreme, the government-owned Citizens National Bank (CNB) which operates primarily in the unorganized subsector of small-scale enterprises and provides consumer loans and small domestic currency loans to firms of an individual, household or cottage type. MIB caters mainly to the needs of modern medium-sized firms, but is also expected to have a significant impact on smaller companies as well.

4.16 The MIB Act confines MIB's financing to "small and medium enterprises" as officially defined by the Presidential Decree enforcing the Act (see para. 2.01). Since MIB's inception in 1961 through 1976, SMI enterprises, i.e. those eligible for MIB's financing, were defined as those with total assets not exceeding W 50 million or with less than 200 employees.^{/1} A Presidential Decree of January 18, 1977, changed these limits to W 500 million and 300 employees ^{/1} respectively, to take into account the steady increase in the size of SMI enterprises in Korea since 1961. Within the SMI sector, no official distinction is made between "small" and "medium." As mentioned earlier in para 2.01, the alternative eligibility criteria for MIB subborrowers in terms of either employment or asset size may be a cause for distortion when the asset limit is set too low, as was the case until January 1977. The alternative employment criterion can then be applied, which may lead to the financing of relatively large, capital-intensive units. In view of this shortcoming, foreign lenders to MIB, who usually regard asset size

^{/1} The employees and assets limits mentioned in this paragraph apply to manufacturing enterprises, which constitute the overwhelming bulk of MIB's portfolio. Slightly different limits are set for other SMI activities such as mining, transportation, trade and services. The employment and asset size limit apply at the time of application for financing by MIB.

as a more meaningful criterion for the definition of SMI often have imposed a single asset limit on the use of their funds. In recognition of the fact that direct foreign exchange financing is in greater demand by enterprises at the medium end of the SMI spectrum this limit normally is higher than the asset limit applied for domestic currency borrowers. Under the first Bank loan to MIB the asset limit was set at W 600 million. Under the proposed loan the limit would be raised to W 1 billion (US\$2 million) in line with the ceiling agreed to by ADB under its latest line of credit. The two size limits mentioned above (W 500 million and 300 employees) constitute an official demarcation of functions between MIB and KDB, in that an enterprise qualifying under either of these two limits (assets or employees) is eligible for borrowing from MIB but not from KDB, and conversely an enterprise exceeding both size limits is eligible for borrowing from KDB but not from MIB. When an existing MIB client has grown to exceed both size limits, it becomes ineligible for MIB's financing and eligible for KDB's financing. The demarcation of functions between MIB and CNB derives from the official restrictions put on CNB's financing, of which the principal ones are: (a) CNB is not allowed to lend to enterprises with more than 100 employees; (b) CNB is not authorized to make (domestic currency) loans in excess of W 30 million; and (c) CNB is not empowered to deal in foreign exchange, thus leaving foreign exchange lending to MIB for the entire SMI sector. In practice, CNB concentrates on the informal/cottage subsector of small industry, while MIB operates in the organized, relatively modern subsector. The foregoing indicates that MIB is the predominant institutional source of domestic currency term finance and, in effect, the sole source of foreign exchange for small and medium-scale industries in Korea.

Overall Lending Operations

4.17 Overview. The most noteworthy feature of MIB's financing activity is that it is geared to meet both the long-term and short-term resource requirements of its clients. MIB's long-term financing consists of equipment (term) loans in both foreign and domestic currencies. Its short-term financing comprises three types of accommodation: discounting of trade bills, overdrafts and general working capital loans. The latter two categories account for the great bulk of MIB's short-term operations and are financed from deposits while bill discounting is financed through the Bank of Korea's rediscounting facility. As of June 30, 1977, MIB had a total outstanding portfolio of W 266 billion (or about US\$548 million). Equipment loans (W 82.3 billion or US\$170 million equivalent) accounted for roughly 31% of the total with foreign exchange equipment loans representing about 56% of total term loans outstanding. MIB's cumulative commitments of equipment loans since its inception in 1961 to June 30, 1977, totaled W 151.4 billion (US\$312 million equivalent), of which foreign currency loans accounted for W 67.8 billion (US\$140 million). MIB began lending in foreign currency in 1965, but substantial foreign exchange resources became available to it only in 1973 with its first loan from the ADB. MIB estimates that its disbursements for equipment loans, which totaled W 70.5 million over the three-year period 1974-76, accounted for about 23% of SMI fixed investment during that period. MIB's extensive coverage of the SMI sector is reflected in the fact that, as of June 30, 1977, its clients numbered over 15,000, or almost 70% of the total number of SMI enterprises (slightly below 22,000) operating in Korea.

4.18 Recent Operational Performance. Except for 1975, MIB's commitments for equipment loans (both foreign and domestic currencies) have rapidly increased in recent years. From a level of W 6.1 million in 1972, these commitments increased by an average of 50% p.a. to W 32.3 billion in 1976. The growth pattern of commitments has, however, been irregular with sharp increases of 180% in 1973 and 85% in 1976 compensating a modest 15% growth in 1974. The annual level of MIB's commitments of term loans has generally been a function of the availability of resources. The decline in commitments in 1975, following a sharp increase during 1972-74, was attributable to a shortage of long-term won resources made available by the Government to MIB. Conversely, the significant expansion (by 85%) of commitments in 1976 was made possible by the availability of the first IBRD loan (which became effective in January 1976), a cash subscription of W 5 billion to MIB's share capital by the Government and an unusually high level of collections on domestic currency loans (W 11.6 billion, against W 4.2 billion in 1975). The fact that MIB was able to increase fivefold the volume of its annual commitments for equipment loans over the four-year period 1972-76 clearly indicates the magnitude of the demand from SMI for its financing. Assuming the availability of adequate resources, MIB should face no difficulty in continuing to expand its term financing at a rate which it projects at around 25-30% p.a. over the next several years.

4.19 MIB's lending for working capital has been growing steadily at a pace of about 27% p.a. since 1972, with the outstanding working capital loan portfolio (a more meaningful indicator than the level of commitments, due to the short maturities and the rollover of funds) rising from W 59.6 billion in 1972 to W 183.7 billion at end-June 1977. This increase in MIB's working capital financing reflected the growth of deposits (by an average of 23% p.a. over the same period) which represents the main source of funds for these operations. MIB's loan operations from 1974 to June 30, 1977, are summarized in Annex 4.

Characteristics of MIB's Lending Operations

4.20 Sectoral Distribution. The manufacturing sector accounted for 91% of MIB's total outstanding portfolio as of June 30, 1977 and close to 99% of all equipment loans outstanding. The nonmanufacturing sectors (construction, transportation, services, and commerce) accounted for only 9% of all outstanding loans and 96% of MIB's assistance to these activities was in the form of working capital loans/¹ (hence the fact that nonmanufacturing accounted for about 1% of equipment loans outstanding). Within the manufacturing sector, textiles and metal products/machinery are the two most important subsectors in MIB's portfolio. Textiles and garments accounted for 31% of the outstanding portfolio at end-June 1977 and fabricated metal products/machinery for 21%; chemicals/rubber/plastics was the next largest subsector with 11% of all loans outstanding. The industrial distribution of MIB's portfolio has remained practically unchanged over the last two years.

4.21 The concentration of about one half of MIB's total portfolio and about 70% of its portfolio of equipment loans, in the two subsectors of textiles and metal products, does potentially expose MIB to the risk of

¹ On an outstanding basis as of June 30, 1977.

cyclical or external factors affecting the performance of these industries. No such risk exists at present and although a sectoral distribution of MIB's arrears shows that textiles accounted for 41% of all arrears at end-June 1977, a higher proportion than their 31% share of outstanding loans, the portfolio of textile loans affected by arrears was less than 9% of all outstanding loans to textile industries, which is low.

4.22 The relatively heavy concentration of MIB's portfolio in textiles reflects to a degree MIB's emphasis (as embodied in both its Act and its Policy Statement) on assisting export-oriented and labor-intensive industries. Textiles meet both criteria well. Of the 62 textile projects financed by MIB under the first Bank Loan, No. 1175, 51 (or 82%) are expected to export at least one half of their output. The 36% share of textiles in Korea's total exports for 1975 exceeded their 31% share in MIB's portfolio of equipment loans. Textile projects financed by MIB in 1976 generated jobs at an average gross capital cost of US\$4,360, which is well below both the Bank's UPP threshold for Korea (US\$5,120 at 1976 prices) and the average gross capital cost per job (US\$8,700) of all MIB's projects financed under the first Bank loan (para. 4.28).

4.23 It would be impractical and perhaps unwise for MIB to curtail its financing of textiles in an attempt to achieve a more balanced sectoral distribution of its portfolio, irrespective of the actual demand for funds. While MIB is concerned about the present portfolio concentration in textiles, its management takes the reasonable view that there is no ground for MIB to reduce lending to this activity as long as Korea remains competitive in export markets by upgrading the quality of its products and diversifying its markets. Under Korea's Fourth Five-Year Plan, the share of textiles in total exports is projected to decline from 36% in 1975 to 26% by 1981, and its share in Korea's total manufacturing investment is also expected to decline marginally, from 23% to 21%. In keeping with this prospective evolution, the share of textiles in MIB's financing is also expected to decline marginally in the years ahead.

4.24 Size Distribution. While the average size of MIB's working capital loans increased from just over W 3 million (US\$6,200) in 1974-75 to about W 6 million in 1976-77, the average size of equipment loans has shown a downward trend from W 22 million (US\$45,000) in 1974 to W 16 million (US\$33,000) in 1977 for domestic currency equipment loans and from W 98 million (US\$200,000) to W 61 million (US\$125,000) for foreign currency loans. In parallel with this downward trend in the size of individual loans there has been a sizable general reduction in the average maturity of all types of loans. The average duration of working capital loans^{/1} has declined from a 2.1 month average in 1974 to 1.6 months in 1976-77 and the weighted ^{/2} average maturity of domestic

^{/1} Based on the ratio of total annual commitments to end-year outstanding balance.

^{/2} By amount.

and foreign currency equipment loans has declined respectively from 7.7 years to 4.3 years and from 8.7 years to 6.9 years. Both of these trends may be an indication of the fact that MIB has been facing a relative shortage of funds over the past years and has consequently tried to reduce loan amounts and to tighten maturities in order to increase the rollover of its funds (at least in the case of domestic currency loans).

4.25 Geographic Dispersal. A significant shift occurred between 1974 and 1977 in the geographic distribution of MIB's financing. While Seoul City accounted for as much as 50% of MIB's outstanding portfolio at end-1974, its share had been reduced to 37% by end-June 1977. Conversely the share of the surrounding Kyung-Gi Province increased from 5% to 17%. Pusan City's share remained stable at 12% throughout that period, as did its surrounding area (South Kyung-Sang Province) with 4% of MIB's portfolio. Taegu, the third major industrial area in Korea (North Kyung-Sang Province) which is an important textile center marginally increased from 13% to 14%. This geographic pattern is generally in line with the present distribution of Korean industry.^{/1} The transfer of industries from Seoul proper into the surrounding province of Kyung-Gi, while other regions maintained their share of industrial investment, is the result of adequate government incentives and policies. MIB has done well in implementing the policy guidelines embodied in its Development Strategy Statement for 1976-77 which emphasized the need for a greater geographic dispersal of its financing. Also in line with this emphasis, MIB has been financing about 50% of all the Saemaeul rural industries established since the introduction of the Government's program in 1973 and lending ceilings have been raised for branches located in the less developed areas ^{/2}. Other relevant characteristics of MIB's loans are shown in Annex 5.

Guarantee Operations

4.26 MIB's guarantee operations are undertaken as a part of the services it renders to its borrowers in connection with its commercial banking activities. Since 1976, almost all the guarantees issued have been short-term guarantees against trading documents, payment of import duties, etc. Long-term guarantees are issued mainly to other financing institutions lending to clients of MIB whose collateral is already pledged to MIB. Since 1976, issuance of such long-term guarantees has been negligible. Outstanding guarantees amounted to W 4.7 billion as of June 30, 1977 (Annex 6).

Equity Operations

4.27 MIB does not intend, in the immediate future, to undertake such operations. First, most small entrepreneurs in Korea do not welcome insti-

^{/1} Seoul and Pusan together accounted for 46% of industrial employment, 43% of value added and 37% of fixed investment in 1975.

^{/2} A loans/deposits ratio of 150% is applied, as compared with 90% for branches in the main three industrial areas.

tutional equity participation; they do not keep accurate financial information on which institutions like MIB can rely and their accounts are rarely audited. Second, MIB's management (quite rightly) believes that the amount of manpower effort that would be needed to monitor SMI equity investments would be totally disproportionate to the benefits realized either by the enterprise or by MIB. Third, neither MIB's financial structure nor its management/staff orientation allow it to engage in operations as inherently risky as providing venture capital. Finally, a considerable gap in providing sufficient debt finance on reasonably secure terms needs to be bridged before riskier equity operations can be contemplated by MIB.

Utilization of Bank Loan No. 1175-K0

4.28 As of June 30, 1977, MIB had approved 132 subprojects for financing under Bank Loan No. 1175-K0 for a total amount of US\$26.9 million. (Since then, the loan balance of US\$3.1 million has been fully allocated on account of six other subprojects.) Subloans ranged in size from US\$31,000 to US\$985,000 with an average of US\$204,000. Bank funds accounted for 46% of the total investment cost of these projects and for 76% of the fixed assets costs. An aggregate amount of US\$16.1 million (close to 60% of total loan amount) was committed for projects in the textiles subsector. The subprojects are expected to generate a total of 6,665 new jobs at an average capital cost of US\$8,700 per job.

4.29 The poverty threshold for Korea has been estimated by the Bank at about US\$5,100 for 1976 which roughly coincides with the period of commitment under Loan 1175-K0. Available data on the subprojects financed under the previous loan show that projects with a cost per job below US\$5,000 (which could, therefore, be construed as conforming with the Bank's Urban Poverty Program), accounted for approximately 20% of the total loan amount. In terms of size of the subborrowers, approximately 11% of the loan amount went to subprojects with fixed assets (including the fixed assets financed under the proposed subloans) below US\$250,000. These figures show that MIB's financial assistance has not been unduly skewed towards the "medium" end of the industrial spectrum at the expense of the "small" end.

Extension Services

4.30 Shortly after its establishment, MIB started providing managerial assistance to Korean SMI on a limited basis. Subsequently, it expanded the scope of its technical assistance to SMI to cover technical consultancy as well. This was achieved with the technical and financial assistance of the United Nations Development Program (UNDP) and of the International Labor Organization (ILO), which, between 1968 and 1974, made available to MIB the services of a number of expatriate advisors and experts. At the same time these experts helped train MIB's staff, and a specialized Extension Services Department (ESD) was established in charge of managerial, financial and technical consultancy services for small and medium enterprises irrespective of whether or not they were borrowers of MIB. Following the departure of the UNDP/ILO experts in 1974, the ESD became understaffed and consultancy services declined from their early 1970s level. At the time of appraisal of the previous Bank loan, MIB acknowledged that the ESD needed both qualitative

and quantitative strengthening, especially in the light of the specific objective outlined in the 1976-77 Development Strategy Statement to intensify extension services. In accordance with that objective, MIB has increased the staffing of the ESD from 34 in 1974 to 38 in 1976 and 45 at end-June 1977. This net increase was achieved in spite of the relatively high number of technical specialists who have left MIB to join private industries.

4.31 MIB's consultancy services range from assistance on minor technical and/or managerial problems which can be solved by correspondence to plant visits by MIB's staff in the branch offices (for relatively simple problems) or in the Extension Services Department (for more complex problems). MIB's technical consultancy covers a variety of subjects including textiles, electrical engineering, metallurgy and mechanical engineering. Managerial assistance includes product management, accounting, inventory control, marketing, etc. In addition, the ESD staff are called upon to conduct professional seminars, to prepare feasibility studies for individual subprojects and to produce various professional publications which are circulated among the Korean small business community.

4.32 In spite of the strengthening of the ESD's staff, the number of field visits, professional seminars and other consultancy services has considerably declined in recent years/¹ and MIB's assistance is now confined to MIB's own clients. Even though larger, more sophisticated firms are now in a position to obtain technical services from private consulting firms against payment of a fee, there is clearly a gap between the needs of the 22,000 SMI firms operating in Korea in 1975 and the 155 cases handled by ESD during that year. The fees charged by MIB for extension services are nominal and do not allow full recovery of the costs involved. A full-scale organization for providing adequate extension services with experienced professionals, however, is a high-cost operation which could seriously impair MIB's profitability. The Government is aware of the existing gap in the provision of adequate technical assistance to SMI and realizes that MIB might not be the best channel. The Government is currently considering a major reorganization of the administrative departments and agencies dealing with SMI, which is likely to involve a reexamination of the system for delivery of extension services to SMI (para. 2.15).

C. Financial Position and Resources

Assets and Liabilities Structure

4.33 Assets. MIB's balance sheets for the years 1974 through June 30, 1977 appear in Annex 8. As of June 30, 1977, MIB's total assets stood at W 377.8 billion (US\$779 million) following a steady growth averaging 24% p.a. over the last two and a half years. Current assets increased rapidly at an average of 34% p.a and now account for 65% of MIB's total assets as against 52% in 1974.

/¹ In-plant consultancy services reached just over 100 cases in 1976 as against 350 in 1970 and 150 in 1974 and 1975.

Current assets essentially comprise: (a) reserves deposited with BOK against deposits;^{/1} and (b) short-term working capital loans. Both increased rapidly reflecting MIB's success in mobilizing demand and savings deposits, which grew at an overall annual average of 26% (38% for short-term demand deposits). MIB's total loan portfolio, including short-term working capital loans, however, remained at the level of approximately 70% of total assets throughout the two and a half year period ended June 30, 1977.

4.34 Liabilities and Equity. Since the end of 1974, the increase in MIB's assets reached W 164 billion, 74% of which was financed by the growth of MIB's current liabilities, 19% by long-term debt and 7% through increases of equity. Current liabilities, of which short-term deposits accounted for 78% at end-June, 1977, have grown steadily at an average of 36% p.a. over the past 30-month period and have more than doubled. As indicated earlier, short-term deposits increased by an average of 38% p.a. and have actually financed about 60% of the increase in MIB's total assets during that period. Long-term liabilities ^{/2} grew by an annual average of 10% only. The growth of MIB's term debt has been irregular (with a mere 1% increase in 1976 following the 16% increase of 1975) and was entirely due to MIB's drawdown on its foreign currency lines of credit (whose outstanding balance increased by an average of 20% p.a.) and higher savings deposits (which increased by an average of 9% p.a. in spite of a slight decline in 1976). Domestic currency term funding from the Government (including budgetary allocations, NIF and IRF) actually declined in absolute amount from an aggregate of W 27.6 billion at end-1974 to W 26.4 billion by June 1977. This decline in available long-term won resources, however, was more than compensated by the W 10 billion contribution made to MIB's share capital in 1976-77. MIB's equity grew even faster, in relative terms, than current liabilities, with an average 45% annual growth between January 1975 and June 1977. MIB's equity stood at W 17.9 billion (US\$36.8 million) as of June 30, 1977.

4.35 The W 10 billion government contribution to MIB's share capital was paid in by installments in early 1976 and early 1977. As a result, MIB's long-term debt/equity ratio ^{/3} which stood at 17.4:1 at end-1975 had declined to 9.8:1 by end-1976 and 7.4:1 as of June 30, 1977. These contributions to MIB's share capital were made in accordance with the Government's undertaking, recorded in the legal documents under Bank Loan No. 1175-KO, to provide MIB with additional equity capital as needed to enable MIB to maintain its long-term debt/equity ratio within the agreed 10:1 limit. This undertaking was reconfirmed and incorporated in the legal documents under the proposed loan. It is further recommended that the limit of 10:1 be maintained under the proposed loan.

^{/1} Reserve requirements set by BOK are 24% for demand deposits and 17% for savings deposits.

^{/2} Including savings deposits with maturities exceeding one year.

^{/3} Long-term guarantees are included in long-term debt.

4.36 MIB's total debt/equity ratio which stood at 32:1 at end-1974 rose to 39:1 in 1975 but dropped to 26:1 and 20:1 by end-1976 and end-June 1977 respectively, following the W 10 billion increase in share capital. This indebtedness is not excessive for an institution which, unlike most DFCs associated with the Bank, is heavily involved in commercial banking operations and which derives a large part of its resources from deposits, particularly short-term demand deposits. In spite of the growing volume of MIB's current liabilities, a total debt/equity limitation (or alternatively, an additional limitation on short-term indebtedness) appears unnecessary, and would unduly constrain MIB's efforts at mobilizing deposits while only higher amounts of deposits can allow a reduction, in relative terms, of the cost of maintaining MIB's nationwide network of branches and deposit offices. This would also run counter to the Government's objective of intensifying the mobilization of domestic savings by financial institutions. The Government's existing undertaking to maintain at all times MIB's long-term debt/equity ratio within 10:1 adequately covers the need for continually strengthening MIB's equity base in the future. As for financial prudence in handling short-term commercial operations, BOK's reserve requirements (para. 4.33) and the supervision exercised by the Superintendent of Banks are designed to ensure that MIB, like other deposit banks, should at any time have sufficient liquidity to service deposits.

4.37 In spite of the sharp increase in current liabilities, MIB's liquidity ratio remains adequate at 1.1:1 at end-1976 and end-June 1977. A conservative /1 estimate of the debt service cover for term borrowings shows that it satisfactorily ranged from 1.1:1 to 1.2:1 over the past three years.

Earnings Performance

4.38 Income statements and indicators of financial performance for the past three and a half years are shown in Annex 9. For 1976, the latest year for which audited accounts are available, MIB's net profit reached W 612 million, an increase of 18% over 1975, but slightly below the level of 1974. It should be noted that in 1975 and 1976 MIB made substantial provisions for bad debts of W 280 million and W 630 million respectively, which sharply reduced the level of net income. At any rate MIB's profitability is modest, reaching about 0.2% of average total assets in 1975 and 1976 and having declined from 7.7% of average equity in 1975 to 6.3% in 1976 following the large increase in MIB's share capital.

4.39 MIB's low profitability is not attributable to an inadequate gross spread, which in spite of a slight decline from 4.4% in 1974-75 to 3.9% in 1976 remains in line with the spread received by other government-owned banking institutions in Korea. In fact, MIB's gross income from loans, whether expressed in terms of average total assets or as a percentage of the average loan portfolio, has increased sizeably over the past two years, /2 but

/1 Excluding collections of term working capital loans.

/2 From 11.1% in 1974 to 11.9% in 1976 as a percentage of average total assets and from 12.8% to 14.6% as a percentage of the average loan portfolio.

this increase was more than offset by a parallel increase in financial expenses, with the result that MIB's spread has remained practically unchanged. MIB's low profitability results from the high level of administrative expenses, particularly salary expenditures, which in turn is attributable to: (a) the wide range of nonprofit development-oriented activities undertaken by MIB partly at the request of Government (e.g. extension services to nonclient companies, assistance to Saemaeul projects, issuance of import licenses, etc.); (b) the mobilization of petty savings from small depositors through a costly nationwide network of branches and deposit offices; and (c) the high overhead usually associated with lending to small-scale enterprises. The level of MIB's administrative expenses compares well with that of other nationwide deposit money banks in Korea.

Portfolio Quality and Provisions

4.40 MIB's portfolio is of unusually good quality considering that MIB operates in the small business sector which is generally considered high-risk, and given its large clientele.^{/1} As of June 30, 1977, total arrears of principal and interest amounted to W 9.2 billion and represented 3.5% of the total short and long-term outstanding portfolio, a level which has remained practically unchanged over the past four years. Principal affected by arrears stood at W 14.5 billion as of June 30, 1977, a slight increase in relative terms over end-1974 from 4.4% of MIB's total portfolio to 5.5%. Owing to the larger average size of term loans, the principal affected by arrears represented 11.4% of equipment loans and 2.8% of working capital loans outstanding. Loans under litigation accounted for about 42% of the total principal in arrears. Debt collection has been highly satisfactory, averaging 91.9% for equipment loans and 99.3% for working capital loans in the past three years. The excellent repayment record of MIB's clients is partly attributable to the strong performance of the Korean economy, particularly in the SMI sector, over the past several years. Annexes 11, 12, and 13 show data on MIB's collection performance and provide an analysis of loans in arrears.

4.41 Loan reschedulings are kept under tight control by MIB's management. On an annual basis, the principal of equipment loans rescheduled accounted for only about 1% of total equipment loans outstanding, and no equipment loan in MIB's portfolio has been rescheduled more than once. The incidence of reschedulings is higher for working capital loans, but this reflects the practice of rollover of loans, which is common in commercial banking. Working capital loans rescheduled during 1976 represented 46% of the year-end outstanding amount. It is, however, more appropriate to relate reschedulings of working capital loans to commitments during the year; the resulting ratio of 6.1% is low. Write-offs have been negligible over the past four years, except in 1976 when they reached W 605 million, or about 0.3% of total outstanding portfolio and 1.7% of MIB's total expenses during that year, which was still moderate.

^{/1} As of June 30, 1977, MIB's portfolio consisted of over 40,000 accounts outstanding with some 15,000 clients.

4.42 Reserves and provisions have remained at about 1.9% of MIB's total portfolio over the past four years but reserves and retained earnings alone account for 95% of the total. Its accumulated provisions for doubtful accounts have so far enabled MIB to cover write-offs without having to reduce its net worth, but provisions accounted for less than 0.1% of the total outstanding portfolio at end-June 1977. In 1975, MIB started to make provisions exceeding actual write-offs in accordance with the agreements reached with the Bank at the time of appraisal of Loan 1175-KO. MIB further undertook during negotiations of the proposed second loan to instruct the external auditors to certify the adequacy of the provisions for bad debts in their audit report for the year 1977 and thereafter based on the auditors' review of MIB's portfolio arrears.

Terms and Conditions of Lending

4.43 The lending rates charged by MIB are not set independently by MIB's Board, but are regulated by the Government through the Monetary Board and apply to all banking and financial institutions. On the domestic currency side, the complex interest rate structure which prevailed through the early seventies has gradually been simplified. A dual rate system still exists with, on the one hand, the "general lending rates" which apply to the operations financed by MIB's own funds, also called banking funds (deposits and equity), and "preferential lending rates" which, on the other hand, are applicable to priority projects financed from governmental budgetary allocations or lines of credit. The "general lending rates" stand since July 1, 1977 at 16% for prime enterprises and 17% for other enterprises in the case of equipment loans; for working capital loans the rates applicable are 17% and 18% respectively. "Preferential lending rates" apply to NIE loans and loans for export industries, both of which are funded by BOK and carry an interest of 13% p.a. and 8% p.a. respectively. Loans for SMI cooperatives and for the modernization of export-oriented SMI are funded by a mix of governmental budgetary resources and MIB's own funds, and carry interest rates ranging from 13% to 13.5%. To the extent that MIB finances such projects with its own resources (which could otherwise be lent at an average of 17%), it receives from the Government an interest subsidy of 3.5% to 4%. On the foreign currency side, MIB normally on-lends the funds with a spread of two percentage points above its own borrowing rate and passes on the foreign exchange risk to its subborrowers. The weighted /1 average interest rate payable on MIB's outstanding domestic and foreign currency borrowings was about 10.1% as of June 30, 1977 which compares with a weighted average lending rate of 15.2% for its outstanding portfolio. The average 5% interest spread on MIB's borrowings is adequate. Maximum maturities on MIB's subloans do not normally exceed 14 years for foreign currency loans, 8 years for domestic currency equipment loans and 3 years for working capital loans.

Audit

4.44 MIB's accounts have been audited since 1965 by Chong Un Accounting Company, a Korean firm associated with Touche Ross & Co. Both in 1975 and

/1 Weighted by outstanding amounts at end-June 1977.

1976, the auditors issued a qualified opinion, pointing out that their interpretation of the implications of MIB's retirement plan showed that the employees' retirement liability had been underestimated. This, however, represented a minor qualification. Other aspects of MIB's accounts were found satisfactory. MIB has since, with the Bank's consent, appointed as its auditors for the year 1977, San Kyong & Co., a company well-known to the Bank. In discussions with San Kyong's representative, the appraisal mission requested that the long form audit report for 1977 specifically address the question of the retirement liability and include a judgment by the auditors on the adequacy of provisions for bad debts based on a review of MIB's accounts in arrears.^{/1} MIB's concurrence with this request was confirmed during negotiations.

Resources

4.45 Domestic Currency Resources. MIB's resource position as of June 30, 1977 is shown in Annexes 14 and 15. Total domestic currency resources amounted to W 300.2 billion (US\$619 million equivalent); deposits amounted to W 240.7 billion, over 80% of the total, while equity and borrowings (from the Government and BOK ^{/2}) accounted for 6% and 14% respectively. W 116.3 billion or 39% of MIB's total domestic currency resources were long-term, of which savings deposits (with maturities exceeding one year) accounted for 62%. Short-term deposits accounted for 92% of MIB's total short-term resources of W 183.9 billion.

4.46 Foreign Currency. The MIB Act was amended in 1964 to authorize foreign currency term lending operations. MIB obtained its first line of credit in foreign currency from KfW of Germany in 1965. By mid-1977, MIB had raised, either directly or through the Government, a total of US\$171.8 million in foreign currency consisting of US\$7 million from USAID, US\$9.6 million from KfW, US\$40.2 million from the Export-Import Bank and OECF of Japan, US\$85 million from ADB (four loans) ^{/3} and US\$30 million under the first IBRD Loan No. 1175-KO. In addition, the Government has made available to MIB foreign currency funds amounting to US\$1.7 million in 1976 and US\$5 million in 1977 thus bringing MIB's cumulative foreign currency resources since 1965 to a total of US\$178.5 million. The US\$1.7 million amount was

^{/1} A review of each account in arrears is feasible if limited to equipment loans. Provisions for working capital loans can be based on past write-off experience.

^{/2} MIB receives from BOK (a) short-term funds to cover its commercial banking operations (essentially discounting of bills); and (b) long-term funds such as NIF borrowings. IRF borrowings which MIB received until 1975 were channeled through KDB.

^{/3} ADB started lending to MIB in 1969; the fourth loan of US\$30 million became effective in April 1977.

part of a US\$6 million line of credit made available to MIB for promoting export-oriented projects of which US\$4.3 million was used to finance commercial imports of raw materials, (these funds were part of a US\$200 million foreign commercial loan raised by the Korean Government in 1976.) The US\$5 million line of credit may, to a limited extent, be used for financing raw material imports as well, but is used by MIB for financing equipment imports since it carries a maximum term of eight years. The latter line of credit is part of the so-called "Korea Foreign Exchange" (KFX) financing scheme sponsored by the Ministry of Finance and funded from the foreign exchange reserves of the Central Bank (BOK). It is expected that a total of US\$500 million will be allocated over the year 1977 primarily to domestic banks dealing in foreign exchange for on-lending to large /1 industrial borrowers at a rate of LIBOR + 1.75%. /2 By making substantial foreign exchange resources available at a relatively low cost to firms which would otherwise rely on foreign commercial sources, pressure is indirectly being exerted to lower the interest rates at which Korean enterprises borrow on the Euro-dollar market to a comparable level. MIB does not deal with large enterprises borrowing on the foreign capital markets /3, and its participation in that scheme is largely a reflection of the Government's concern to increase its assistance to the SMI sector. Additional KFX funds are expected to be allocated to MIB in 1977 and in the future as the need arises.

4.47 As of June 30, 1977, MIB had foreign currency resources available for future commitments amounting to US\$38.6 million. The fourth ADB credit line accounted for most of it (US\$29.6 million) while the balance of Bank Loan No. 1175-K0 and KFX funds amounted to US\$4.6 million and US\$4.2 million respectively.

D. Prospects and Resource Requirements

Business Projections

4.48 MIB's disbursements of equipment loans accounted for approximately 23% of total expenditures on fixed assets in the SMI sector over the past three years. MIB has projected its future operations for the five-year period 1977-81 (Annex 16) on the basis of the following assumptions: (a) SMI fixed investment would increase in current terms by 15% p.a. (or 8% in real

/1 Subloans of up to US\$20 million are authorized under this scheme.

/2 LIBOR + 2% including a guarantee fee of 0.25%.

/3 Lending conditions are different in the case of MIB, e.g. the maximum loan amount is US\$500,000 and terms are slightly longer (eight years including three years grace). The lending rate, however, is the same.

terms assuming an inflation rate of 7% p.a.), the same as the growth rate for investment in the overall manufacturing sector projected in the Fourth Five-Year Plan; (b) MIB's share in the financing of SMI fixed investment would gradually rise from 23% for 1974-76 to 25% in 1977, 27% in 1979 and 33% by 1981; and (c) the proportion of MIB's foreign currency lending in relation to its total equipment (term) financing would gradually decline from 42% for 1974-76 to 40% in 1978 and 37% by 1981, reflecting the steady development of the domestic machinery industry and the resulting increased availability of domestic capital goods. It is expected that, in line with the Government's new emphasis on SMI development, adequate domestic currency financial resources will be made available by the Government (from both budgetary allocations and NIF funding) to MIB to enable it to achieve its projected volume of term lending. In regard to working capital loans, MIB has projected for the same 1977-81 period a growth rate of 30% p.a. in net disbursements, which essentially reflects: (a) the projected growth rate of MIB's deposits, based in turn on MIB's actual deposit growth rate over the past five years; and (b) increased short-term borrowings from BOK.

4.49 Total commitments of equipment loans are projected to increase by 32% in 1977, a higher growth rate than the average 23% projected over the following four-year period owing to the expanded scope of MIB's financing following the revision of the definition of SMI enterprises in January 1977 (para. 2.02) whereby manufacturing enterprises with up to 300 employees (instead of 200 as has previously been the case) now qualify for MIB's financial assistance. Net commitments of working capital loans are forecast to increase by an average annual rate of 30% over the 1977-81 period. Total projected commitments would increase from an actual level of W 57.6 billion (US\$119 million) in 1976 ^{/1} to W 195 billion (US\$402 million) by 1981. Equipment loans (in both foreign and domestic currencies), which accounted for 56% of total commitments, would marginally decline to 51% by the end of the five-year projection period. With its present and prospective staff capacity, MIB should be able to achieve this projected volume of operations.

Resource Requirements

4.50 Domestic Currency Resource Position and Requirements. MIB's cumulative commitments of domestic currency loans are projected to reach a total of W 540.6 billion (US\$1,115 million) over the projection period 1977-81 consisting of W 210.6 billion for equipment loans and W 330 billion for working capital loans. As of December 31, 1976, total domestic currency resources available for commitment amounted to W 20.7 billion of which W 8.3 billion were short-term resources. MIB plans to raise a total of W 207.4 billion in long-term domestic currency resources and W 367.5 billion in short-term resources over the five-year period 1977-81 as follows:

^{/1} Including net increase in commitments of working capital loans.

	Domestic currency requirements				
	-----W billion-----				
	1977	1978	1979	1980	1981
<hr/>					
<u>Long-term resources</u>					
Uncommitted resources	12.4	9.9	10.5	16.0	12.3
Cash generated from operations	1.4	2.0	4.0	6.2	8.4
Share capital increase	5.0 <u>/a</u>	7.0	9.9	-	-
Government borrowings	2.0	2.5	3.1	3.9	4.9
National Investment Fund	7.0	8.4	10.1	12.1	14.5
Net won term loan collections <u>/b</u>	<u>7.2</u>	<u>12.7</u>	<u>18.6</u>	<u>24.4</u>	<u>32.0</u>
Subtotal	<u>35.0</u>	<u>42.5</u>	<u>56.2</u>	<u>62.6</u>	<u>72.1</u>
New commitments of equipment loans	25.1	32.0	40.2	50.3	63.0
Uncommitted balance at year-end	9.9	10.5	16.0	12.3	9.1
<u>Short-term resources</u>					
Uncommitted resources	8.3	16.5	20.9	20.7	32.8
Borrowings from BOK (net)	10.2	13.3	17.2	22.4	29.1
Net increase in short-term deposits <u>/c</u>	22.2	22.8	18.0	30.2	35.1
Net increase in savings deposits <u>/d</u>	<u>15.0</u>	<u>19.8</u>	<u>33.1</u>	<u>34.5</u>	<u>44.6</u>
Subtotal	<u>55.7</u>	<u>72.4</u>	<u>89.2</u>	<u>107.8</u>	<u>141.6</u>
New working capital loans commitments	39.2	51.5	68.5	75.0	95.8
Uncommitted balance at year-end	16.5	20.9	20.7	32.8	45.8

/a Already paid-in by Government in early 1977.

/b Net of repayments of long-term domestic currency borrowings.

/c Net of BOK reserve requirements.

/d Net of BOK reserve requirements and subscription to NIF debentures.

4.51 Of the total W 207.4 billion term resources which MIB plans to raise, an amount of W 90.4 billion or 44% is expected to be provided by the Government consisting of: (a) W 21.9 billion ^{/1} as additional contributions to MIB's share capital; (b) budgetary allocations totaling W 16.4 billion; and (c) W 52.1 billion through NIF borrowings. The level of financing which MIB hopes to receive from the Government exceeds that of the past few years but does not appear unrealistic considering the Government's intention to enhance its financial assistance to Korean SMI, particularly through MIB.

4.52 Foreign currency resources. During the first half of 1977, MIB committed only US\$9.4 million (W 4.6 billion) out of total projected commitments of US\$36 million for 1977. The 1977 target, however, does not appear unreasonable given that: (a) it represents a 29% increase over the 1976 commitments of foreign currency loans, which is in line with the 30% average annual growth rate of commitments over the period 1974-76; (b) fixed assets investment in 1975 by SMI manufacturing enterprises employing between 200 and 300 persons (the new limit of eligibility for financing by MIB since January 1977) represented about 29% of total fixed investment by enterprises employing less than 200 persons (the former limit); and (c) MIB's uncommitted approvals of foreign currency loans amounted to US\$13.6 million as of June 30, 1977. Over the period July 1977-December 1981, total commitments of foreign currency loans are expected to reach a total of US\$261 million, an average of about US\$58 million per year. Table 4.15 shows that as of June 30, 1977, MIB had foreign currency resources available for further commitment amounting to US\$38.6 million.^{/2} In order to cover the projected level of operations, MIB would therefore need to borrow about US\$222 million. MIB hopes to secure approximately US\$200 million over that period by borrowing from the Bank and ADB in alternative years. The balance is expected to be covered by additional lines of credit to be made available by the Korean Government under the KFX scheme (see para. 4.46).

Financial Forecasts

4.53 MIB's projected balance sheets, income statements and financial ratios for the years 1977-81 are shown in Annexes 17, 18 and 19. Net income is expected to increase from W 0.78 billion in 1977 (0.2% of average total assets) to W 7.1 billion by 1981 (0.7% of average total assets) which is probably an optimistic assumption. While financial expenses are expected to remain close to their 1976 level of 8% of average

^{/1} Of which W 5 billion have already been paid in by the Government in early 1977.

^{/2} Approximately US\$12 million would be left by end-1977, enough to cover projected commitments in the first quarter of 1978 before the proposed Bank loan comes on stream.

total assets, gross income would increase marginally from 11.9% in 1976 to 12.4% by 1981 as balances of low interest yielding loans made in earlier years decline. MIB's gross spread would consequently increase from about 4% in 1976 to 4.5% in 1981. Administrative expenses are expected to remain at their 1976 level of 3.5% to 3.6% of average total assets. With provisions and income tax at about 0.1%, the increase in MIB's gross spread would result in a parallel increase of net income from 0.2% of average total assets in 1976 to 0.7% in 1981.

4.54 The growth of MIB's net income is likely to prove more moderate than is projected if, as is desirable, the annual level of provisions is increased to provide for a gradual accumulation of provisions instead of being based solely on projected write-offs for the following year. An understanding was reached in 1975 that, the excellent quality of its portfolio notwithstanding, MIB would start accumulating provisions in accordance with sound banking practice so as to enable it to write off bad debts without having to deplete its equity in the event that, due to unforeseen circumstances, bad debts were to exceed past historical levels. MIB has adhered to this understanding over the past two years and its annual provisions exceeded the level of actual write-offs. Assurances were obtained from MIB at negotiations that the adequacy of provisions for bad debts will be certified by its external auditors in their annual audit report on MIB's accounts.

4.55 Total assets are forecast to increase from W 342.2 billion at year-end 1974 to W 1,055 billion (over US\$2 billion) in 1981, an average growth rate of 25% p.a. MIB's total loan portfolio would also grow at an average annual rate of 25% and therefore retain its 1976 level of about 70% of total assets throughout the projection period. Equipment loans are expected to marginally increase as a share of total assets from 22.2% in 1976 to 23.9% in 1981. The ratios of financial performance and structure show a satisfactory and improving trend. MIB's liquidity position is expected to improve, with the current ratio increasing from 1.12 in 1976 to 1.31 in 1981. The long-term debt/equity ratio which stood at 9.8:1 as of end-1976 is expected to decline to 8.6:1 by end-1977 (as the result of the W 5 billion increase in MIB's share capital earlier in the year) and to further decline in 1978 and 1979 with additional cash subscriptions to MIB's share capital by the Government. It would then increase in 1980/81 and reach 9.6:1 by end-1981 which would still be within the contractual limit of 10:1. The debt service cover is expected to gradually improve from 1.2 in 1976 to 1.4 in 1981.

5. THE PROPOSED BANK LOAN

Recommendation and Justification

5.01 MIB's performance in the past two years has been highly satisfactory from both the institutional and developmental standpoints, generally living up to the expectations set out by the Bank at the time it approved its first loan to MIB. With its operational capability, including its satisfactory project appraisal and follow-up work, MIB is a particularly suitable allocator of Bank resources to SMI enterprises in Korea. A new Bank loan of \$55 million is recommended, which is expected to cover slightly more

than one half of MIB's foreign currency commitments over a two-year period 1978-1979, with the balance to be met with additional borrowings from other sources including the Asian Development Bank.

5.02 One specific and important objective under the first Bank loan to MIB was to enable the Bank to assist small industrial projects in Korea which, owing to their size, are not usually financed by the other two financial intermediaries assisted by the Bank, namely KDFC and KDB. This objective has, by and large, been achieved. For the 132 projects financed by MIB under the first Bank loan, the average subloan size was about US\$210,000, the average cost of the projects financed US\$0.4 million and the average total assets of subborrowers US\$0.6 million. By comparison, the average size of KDFC's subloans in 1976 was about US\$1.0 million, the average cost of its projects US\$3.0 million and the average total assets of its subborrowers US\$5.0 million. KDB's projects are generally comparable to, or larger than, KDFC's. Apart from being much smaller, MIB's projects are also considerably more labor-intensive than KDFC's and KDB's. The average gross capital cost per job of the above-mentioned 132 MIB projects was US\$8,700, which was not substantially higher than the Bank's UPP threshold for Korea of US\$5,120 on the basis of 1976 prices. (By comparison, the average gross capital cost per job for projects financed by KDFC in 1976 was US\$21,500). MIB's subprojects under the first Bank loan were also highly export-oriented, with about 55% of their output expected to be sold on export markets. Although MIB does not routinely calculate the economic rates of return (ERR) of the projects it finances, an ex-ante calculation on a representative sample of 20 projects approved by MIB in 1974 shows ERRs in excess of 30% and financial rates of return in excess of 20% for a vast majority of these projects.

5.03 The foregoing indicates that Bank funds put at MIB's disposal have been allocated to industrial projects which are financially as well as economically viable, especially in terms of export earnings and employment generation. The projects to be financed under the proposed loan are expected to achieve similar or greater financial and economic benefits. Lending to MIB represents an efficient means of transferring Bank resources to Korea's key industrial sector and enables the Bank, through a continuing relationship, to deepen its institution-building impact on MIB which started in 1975 with the first Bank loan.

Main Features of the Loan

5.04 Component for Financing Projects Addressing the Alleviation of Urban Poverty. As noted in para. 5.02 and elsewhere in this report, MIB has achieved satisfactory results in terms of allocating the proceeds of the first Bank loan to small entrepreneurs and labor-intensive projects. It is important that under the proposed loan MIB should continue or even intensify its endeavor to reach smaller enterprises (in terms of total assets) and finance more labor-intensive projects (as measured by the capital/labor ratio). This would be consistent with both the Government's new emphasis on small-scale enterprises and the Bank's objective of contributing to the alleviation of poverty through the financing of labor-intensive investment projects.

Toward that objective, it is recommended that a component of US\$20 million (or 36% of the proposed loan amount of US\$55 million) be earmarked for financing specifically: (a) projects which create employment at a gross capital cost per job not greater than US\$6,000; or (b) enterprises with fixed assets not exceeding US\$250,000. The proposed US\$6,000 capital/labor limit is slightly higher than the Bank's UPP threshold for Korea of US\$5,120 on the basis of 1976 prices, but appears appropriate considering that MIB's commitments under the proposed loan will take place in 1978-1979 and taking into account the inflation factor. The proposed US\$250,000 fixed assets ceiling coincides with that suggested for small-scale enterprise lending in the recent Bank report entitled "Employment Creation and Small-Scale Enterprise Development" (No. 1543 dated March 22, 1977). Based on an analysis of the available data on the 132 subprojects financed under the first Bank loan (para. 5.02), MIB is expected, with a reasonable but not excessive effort on its part, to be able to fully utilize the special component as described above.

5.05 Financing of Foreign Exchange Component of Domestic Equipment.

Aside from the financing of direct imports of machinery and equipment, it is recommended that MIB be authorized to use the proceeds of the proposed loan for financing the foreign exchange component of domestically manufactured capital goods estimated at 60%. This authority should enhance MIB's potential for financing smaller projects under the proposed loan in view of the fact that such projects often require domestically produced, rather than imported, capital goods.

5.06 Free Limit. It is recommended that the free limit of US\$0.5 million, set under the previous Bank loan, be maintained. The maintenance of the free limit does not imply any dissatisfaction with MIB's project appraisal work which remains satisfactory. It rather reflects the recognition that the previous free limit of US\$0.5 million was on the high side, as evidenced by the small number (3 out of 132) of projects above the free limit under the first Bank loan.

5.07 Ceiling on Subloans and Size of Subborrowers. Under the previous Bank loan, a ceiling of US\$1 million on individual subloans and a limit of W 600 million on total assets of eligible subborrowers, were set. It is recommended that these figures be raised respectively to US\$1.5 million and W 1 billion under the proposed loan (outside the special component referred to in para. 5.04 above), to bring them in line with the Government's recent decision increasing the total assets limit for borrowers eligible for MIB's foreign exchange financing (para. 4.16), and to take into account the steady expansion in the size of industrial projects/enterprises in Korea.

5.08 Debt/Equity Limit. Under the first Bank loan, a limit of ten times its equity was set on MIB's long-term debt, (with all government loans and all deposits with maturity exceeding one year to be included in debt.) Furthermore, the Government undertook specifically, (as recorded in the Guarantee Agreement), to provide MIB with additional equity capital as needed in future to enable MIB to keep its debt/equity ratio within the 10:1 limit (para. 4.35). It is recommended that this debt/equity limit be maintained under the proposed loan, and that the Government's undertaking as described above be recorded again in the Guarantee Agreement.

5.09 Relending Rate. MIB intends to relend the proceeds of the proposed loan at a rate of 9.9%, which would give it an adequate spread of 2 percentage points (assuming a Bank lending rate of 7.9%). The two percentage point spread over MIB's own borrowing rate is in line with the practice of government-owned development institutions such as MIB and KDB in relending the proceeds of their borrowings from institutional sources (ADB, IBRD, et al.). The spread is adequate to cover the cost associated with the processing of foreign currency lending. The onlending rate to the subborrowers of about 10% p.a. represents a positive real rate of interest provided the Government is able to maintain inflation at the rate of 7% p.a. projected in the Fourth Five-Year Plan. Should the Government fail to achieve this objective and inflation in Korea exceed present projections, adjustments of the won/dollar exchange rate could be expected to take place which, considering that sub-borrowers will bear the foreign exchange risk, would maintain the real interest rate at a positive level. Over the period 1960-76, when inflation ran at an average of 15% p.a. the depreciation of the won vis-a-vis the dollar averaged 7% p.a.

5.10 Amortization Schedule. As usual with Bank loans to DFCs, the proposed loan would have a flexible amortization schedule conforming substantially with the aggregate of the repayment schedules of the subloans made by MIB. The loan is expected to be fully repaid within a period of 17 years including a grace period of 3 years. The estimated disbursement schedule of the loan is shown in Annex 22.

Agreements and Understandings Reached at Negotiations

5.11 During negotiations, the Bank reached agreement:

- (a) with the Government (recorded in the Guarantee Agreement) to the effect that it will continue to provide MIB with additional equity as needed in future to keep MIB's debt/equity ratio within the 10:1 limit (para. 4.35);
- (b) with MIB on:
 - (i) the maintenance of the long-term debt/equity limit at 10:1 (para. 4.35);
 - (ii) a component of US\$20 million within the loan for financing projects that would create employment at a gross capital cost per job not greater than US\$6,000, or for enterprises with fixed assets not exceeding US\$250,000 at the time of submission of the loan application to MIB (para. 5.04);
 - (iii) a percentage of 60 representing the foreign exchange component of domestically procured capital goods (para. 5.05);
 - (iv) the maintenance of the free limit at US\$0.5 million (para. 5.06); and
 - (v) a US\$1.5 million ceiling on individual subloans and a limit of W 1 billion on total assets of eligible borrowers (para. 5.07).

5.12 In addition, the following matters were reviewed with MIB at negotiations:

- (a) the objectives outlined by MIB in its statement of Development Strategy for 1978-79 (para. 4.10); and
- (b) MIB's plans for establishing provisions for bad debts (para. 4.42).

KOREA

MEDIUM INDUSTRY BANK

Composition of MIB's Board of Policy
(As of June 30, 1977)

1. Nam, Sang Jin - President of the Medium Industry Bank
2. Ha, Dong Sun - Director, Finance Bureau, Ministry of Finance
(Nominated by the Minister of Finance)
3. Kim, Jong Hak - Director, Bureau of Small and Medium Industry,
Ministry of Commerce and Industry
(Nominated by the Minister of Commerce and
Industry)
4. Cho, Chun Shik - Assistant Governor, The Bank of Korea
(Nominated by the Governor of the Bank of Korea)
5. Kim, Bong Jae - Chairman, National Federation of Small and Medium
Industry Cooperatives
6. Choi, Ik Sung - Director, National Federation of Small and Medium
Industry Cooperatives (Representative of small
entrepreneurs)
7. Lee, Kwan Soo - Chief of Directorate, Korea Stationery Industry
Cooperative (Representative of small entrepreneurs)

KOREAMEDIUM INDUSTRY BANKComposition of MIB's Board of Directors
(As of June 30, 1976)

<u>Name</u>	<u>Position</u>	<u>Background</u>
1. Nam, Sang Jin	President	Appointed May 12, 1976. Previously Vice Minister, Ministry of Finance
2. Park, Sung Sang	Deputy President	Appointed November 18, 1976. Previously Assistant Governor, The Bank of Korea
3. Kim, Chong Hwan	Director	Previous commercial banking background. Joined MIB in 1961. Appointed Director in 1972. Re-appointed in April 1975.
4. Kim, Jae Sup	Director	Previous commercial banking background. Joined MIB in 1961. Appointed Director in 1974. Re-appointed in February 1977.
5. Choi, Heung Sik	Director	Previous commercial banking background. Joined MIB in 1961. Appointed Director in 1974. Re-appointed in February 1977.
6. Park, Chu Hee	Director	Previous commercial banking background. Joined MIB in 1961. Appointed Director in April 1975.
7. Park Jang Shur	Director	Previous commercial banking background. Joined MIB in 1961. Appointed Director in April 1975.

KOREAMEDIUM INDUSTRY BANKPartial Economic Indicators of Foreign Currency Loans Approved, 1973-1976 /a

	1973/74	1975	1976	1973-76
Number of projects	174	121	127	422
Total project cost (W million)	33,611	29,432	31,442	94,485
Amount of MIB's financing (W million)	15,399	12,435	16,892	44,726
Share of MIB's financing (%)	45.8	42.2	53.7	47.3
Incremental annual sales (W million)	70,037	55,870	63,414	189,321
Incremental annual value added (W million)	30,392	14,122	17,343	61,857
Direct additional employment (number)	22,369	5,241	5,601	33,211
Incremental annual gross exports (\$ million)	79.7	62.8	71.9	214.4
Increase in fixed assets (W million)	24,306	15,336	24,468	64,110

Economic indicators

Sales per employee (W thousand)	3,131	10,660	11,322	5,700
Value added per employee (W thousand)	1,359	2,695	3,096	1,863
Investment per employee (W thousand)	1,503	5,616	5,614	2,845
Ratio of sales to fixed assets	2.9	3.6	2.6	3.0
Ratio of value added to fixed assets	1.3	0.9	0.7	1.0
Ratio of value added to sales	0.4	0.3	0.3	0.3
Export share of sales	55.2	54.5	55.0	54.9

/a Based on projections made at the time of appraisal.

KOREA

MEDIUM INDUSTRY BANK

Summary of Loan Operations, 1974 - June 30, 1977
(In W million)

	1974		1975		1976		1977 (6 months)	
	No.	Amount	No.	Amount	No.	Amount	No.	Amount
<u>Approvals</u>								
Equipment loans								
Domestic currency	461	10,015	337	7,295	1,241	18,755	768	12,129
Foreign currency	95	9,322	136	12,369	167	13,533	166	10,114
Total equipment loans	<u>556</u>	<u>19,337</u>	<u>473</u>	<u>19,664</u>	<u>1,408</u>	<u>32,288</u>	<u>934</u>	<u>22,243</u>
Working capital loans	198,741	610,259	264,641	843,301	190,062	1,174,228	124,320	693,616
Total approvals	<u>199,297</u>	<u>629,596</u>	<u>265,114</u>	<u>862,965</u>	<u>191,470</u>	<u>1,206,516</u>	<u>125,254</u>	<u>715,859</u>
<u>Commitments</u>								
Equipment loans								
Domestic currency	461	10,015	337	7,295	1,241	18,755	768	12,129
Foreign currency	98	9,623	105	10,109	171	13,589	118	4,574
Total equipment loans	<u>559</u>	<u>19,638</u>	<u>442</u>	<u>17,404</u>	<u>1,412</u>	<u>32,344</u>	<u>886</u>	<u>16,703</u>
Working capital loans	198,741	610,259	264,641	843,301	190,062	1,174,228	124,320	693,616
Total commitments	<u>199,300</u>	<u>629,897</u>	<u>265,083</u>	<u>860,705</u>	<u>191,474</u>	<u>1,206,572</u>	<u>125,206</u>	<u>710,319</u>
<u>Disbursements</u>								
Equipment loans								
Domestic currency	-	9,310	-	8,000	-	18,755	-	12,129
Foreign currency	-	11,726	-	10,506	-	13,777	-	6,393
Total equipment loans	-	<u>21,036</u>	-	<u>18,506</u>	-	<u>32,532</u>	-	<u>18,522</u>
Working capital loans /a	-	609,209	-	844,351	-	1,174,228	-	693,616
Total disbursements	-	<u>630,245</u>	-	<u>862,857</u>	-	<u>1,206,760</u>	-	<u>712,138</u>
<u>Repayments</u>								
Equipment loans								
Domestic currency	-	4,032	-	4,184	-	11,632	-	9,521
Foreign currency	-	2,199	-	3,647	-	4,303	-	3,000
Total equipment loans	-	<u>6,231</u>	-	<u>7,831</u>	-	<u>15,935</u>	-	<u>12,521</u>
Working capital loans	-	578,281	-	820,492	-	1,148,988	-	667,833
Total repayments	-	<u>584,512</u>	-	<u>828,323</u>	-	<u>1,164,923</u>	-	<u>680,354</u>
<u>Loans Outstanding</u>								
Equipment loans								
Domestic currency	1,919	22,490	2,139	26,306	2,364	33,429	2,395	36,037
Foreign currency	529	26,530	636	33,389	745	42,863	815	46,256
Total equipment loans	<u>2,448</u>	<u>49,020</u>	<u>2,775</u>	<u>59,695</u>	<u>3,109</u>	<u>76,292</u>	<u>3,210</u>	<u>82,293</u>
Working capital loans /a	34,638	108,811	36,803	132,670	36,207	157,910	37,345	183,693
Total loans outstanding	<u>37,086</u>	<u>157,831</u>	<u>39,578</u>	<u>192,365</u>	<u>39,316</u>	<u>234,202</u>	<u>40,555</u>	<u>265,986</u>

/a Breakdown of working capital loans disbursed and outstanding:

	Discounting		Overdrafts		General working capital loans		Total	
	Disbursed	Outstanding	Disbursed	Outstanding	Disbursed	Outstanding	Disbursed	Outstanding
1974	19,723	4,032	260,144	4,964	329,342	99,815	609,209	108,811
1975	42,002	9,839	425,290	6,463	377,059	116,368	844,351	132,670
1976	74,284	14,199	642,115	9,945	457,829	133,766	1,174,228	157,910
1977 (up to June 30)	51,194	16,351	380,568	14,151	261,854	153,191	693,616	183,693

KOREA
MEDIUM INDUSTRY BANKAnalysis of Loans Outstanding as of June 30, 1977
(in W million)

	Foreign Currency		Domestic Currency		Total Equipment		Working Capital		Total Loans	
	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%
<u>Nature of Projects /a</u>										
New enterprise	6,322	13.7	4,274	11.9	10,596	12.9	33,996	18.5	44,592	16.7
Existing enterprise	39,934	86.3	31,763	81.1	71,797	87.1	149,697	81.5	221,394	83.3
<u>Total</u>	<u>46,256</u>	<u>100.0</u>	<u>36,037</u>	<u>100.0</u>	<u>82,293</u>	<u>100.0</u>	<u>183,693</u>	<u>100.0</u>	<u>265,986</u>	<u>100.0</u>
<u>Sectoral Distribution</u>										
<u>Manufacturing</u>										
Food, beverage and tobacco	2,262	4.9	984	2.7	3,246	3.9	11,541	6.3	14,787	5.6
Textile, wearing apparel and leather	20,926	45.2	16,179	44.9	37,105	45.1	46,366	25.3	83,471	31.5
Wood and wood products	98	0.2	445	1.2	543	0.7	8,622	4.7	9,165	3.4
Paper, paper products and printing	4,035	8.7	270	0.7	4,305	5.2	10,672	5.8	14,977	5.6
Chemicals, petroleum, rubber and plastics	3,471	7.5	4,589	12.8	8,060	9.8	21,321	11.6	29,381	11.0
Nonmetallic mineral products	709	1.5	2,209	6.1	2,918	3.5	9,127	5.0	12,045	4.5
Basic metals	1,142	2.5	1,815	5.0	2,957	3.6	8,644	4.7	11,601	4.4
Fabricated metal products, machinery	11,917	25.8	7,817	21.8	19,734	24.0	36,785	20.0	56,519	21.2
Others	919	2.0	1,559	4.3	2,478	3.0	8,685	4.7	11,163	4.2
<u>Subtotal</u>	<u>45,479</u>	<u>98.3</u>	<u>35,867</u>	<u>99.5</u>	<u>81,346</u>	<u>98.8</u>	<u>161,763</u>	<u>88.1</u>	<u>243,109</u>	<u>91.4</u>
<u>Non-manufacturing</u>										
Mining	322	0.7	30	0.1	352	0.4	1,876	1.0	2,228	0.8
Construction	8	-	12	0.1	20	0.1	845	0.5	865	0.3
Transportation	300	0.7	48	0.1	348	0.4	4,503	2.5	4,851	1.8
Services and commerce	147	0.3	80	0.2	227	0.3	7,895	4.2	8,122	3.1
Other	-	-	-	-	-	-	6,811	3.7	6,811	2.6
<u>Subtotal</u>	<u>777</u>	<u>1.7</u>	<u>170</u>	<u>0.5</u>	<u>947</u>	<u>1.2</u>	<u>21,930</u>	<u>11.9</u>	<u>22,877</u>	<u>8.6</u>
<u>Total</u>	<u>46,256</u>	<u>100.0</u>	<u>36,037</u>	<u>100.0</u>	<u>82,293</u>	<u>100.0</u>	<u>183,693</u>	<u>100.0</u>	<u>265,986</u>	<u>100.0</u>
<u>Geographical Distribution</u>										
Seoul City	17,576	38.0	10,724	29.7	28,300	34.4	71,113	38.7	99,413	37.4
Kyung-gi Province	8,940	19.3	5,004	13.9	13,944	16.9	32,313	17.6	46,257	17.4
South Chung-cheong Province	1,713	3.7	3,196	8.9	4,909	6.0	4,605	2.5	9,514	3.6
North Chung-cheong Province	1,161	2.5	671	1.9	1,832	2.2	4,036	2.2	5,868	2.2
Kang Won Province	90	0.2	448	1.2	538	0.7	4,902	2.7	5,440	2.0
South Jeon-ra Province	945	2.0	1,529	4.2	2,474	3.0	5,676	3.1	8,150	3.1
North Jeon-ra Province	1,065	2.3	1,461	4.1	2,526	3.1	6,197	3.4	8,723	3.3
South Kyung-sang Province	1,436	3.1	1,413	3.9	2,849	3.5	8,082	4.4	10,931	4.1
North Kyung-sang Province	7,828	16.9	6,974	19.4	14,802	18.0	22,479	12.2	37,281	14.0
Pusan City	5,467	11.9	4,468	12.4	9,935	12.0	22,199	12.1	32,134	12.1
Cheju Island	35	0.1	149	0.4	184	0.2	2,091	1.1	2,275	0.8
<u>Total</u>	<u>46,256</u>	<u>100.0</u>	<u>36,037</u>	<u>100.0</u>	<u>82,293</u>	<u>100.0</u>	<u>183,693</u>	<u>100.0</u>	<u>265,986</u>	<u>100.0</u>

/a On a commitment basis, financing of new lines of production during the first half of 1977 represented approximately 22% of total equipment loans.

KOREA

MEDIUM INDUSTRY BANK

Analysis of Loans Outstanding as of June 30, 1977
(In W million)

	Foreign Currency		Domestic Currency		Total Equipment		Working Capital		Total Loans	
	Amount	%	Amount	%	Amount	%	Amount	%	Amount	%
Size of Loans										
Less than W 1 million	3	-	69	0.2	72	-	7,455	4.0	7,527	2.8
From W 1 to 10 million	513	1.1	6,872	19.1	7,385	9.0	131,819	71.8	139,204	52.3
From W 10 to 30 million	5,235	11.3	19,474	54.0	24,709	30.2	34,537	18.8	59,246	22.3
From W 30 to 50 million	7,620	16.5	5,545	15.4	13,165	16.0	6,782	3.7	19,947	7.5
From W 50 to 100 million	12,458	26.9	3,170	8.8	15,628	19.0	1,074	0.6	16,702	6.3
From W 100 to 150 million	9,380	20.3	364	1.0	9,744	11.8	1,482	0.8	11,226	4.2
From W 150 to 300 million	9,617	20.8	543	1.5	10,160	12.3	544	0.3	10,704	4.0
W 300 million and over	1,430	3.1	-	-	1,430	1.7	-	-	1,430	0.6
Total	46,256	100.0	36,037	100.0	82,293	100.0	183,693	100.0	265,986	100.0
Duration										
Up to 1 year	64	0.1	1,171	3.2	1,235	1.5	157,200	85.6	158,435	59.6
1 to 3 years	1,966	4.3	12,456	34.6	14,422	17.5	26,493	14.4	40,915	15.4
3 to 6 years	14,411	31.1	13,856	38.5	28,267	34.3	-	-	28,267	10.6
6 to 10 years	27,398	59.2	8,554	23.7	35,952	43.8	-	-	35,952	13.5
10 to 15 years	2,417	5.3	-	-	2,417	2.9	-	-	2,417	0.9
Over 15 years	-	-	-	-	-	-	-	-	-	-
Total	46,256	100.0	36,037	100.0	82,293	100.0	183,693	100.0	265,986	100.0
Subborrowers Assets Size /a										
Up to W 10 million	-	-	320	0.9	320	0.4	10,209	5.6	10,529	4.0
W 10 to 30 million	225	0.5	3,037	8.4	3,262	4.0	38,419	20.9	41,681	15.7
W 30 to 50 million	2,927	6.3	6,162	17.1	9,089	11.0	41,432	22.6	50,521	19.0
W 50 to 100 million	3,842	8.3	13,040	36.2	16,882	20.5	45,690	24.8	62,572	23.4
W 100 to 300 million	15,170	32.8	9,866	27.4	25,036	30.5	32,720	17.8	57,756	21.7
W 300 to 600 million	15,758	34.1	2,534	7.0	18,292	22.2	10,054	5.5	28,346	10.7
Over W 600 million	8,334	18.0	1,078	3.0	9,412	11.4	5,169	2.8	14,581	5.5
Total	46,256	100.0	36,037	100.0	82,293	100.0	183,693	100.0	265,986	100.0
Type of Borrowers										
Joint stock companies	31,512	68.2	19,019	52.8	50,531	61.4	80,921	44.1	131,452	49.4
Partnerships	64	0.1	746	2.1	810	1.0	1,312	0.7	2,122	0.8
Sole proprietorships	14,540	31.4	15,079	41.8	29,619	36.0	21,448	49.7	121,067	45.5
Cooperatives, etc.	140	0.3	1,193	3.3	1,333	1.6	10,012	5.5	11,345	4.3
Total	46,256	100.0	36,037	100.0	82,293	100.0	183,693	100.0	265,986	100.0
Equipment Loans										
	Foreign Currency		Domestic Currency		Total Equipment		Working Capital Loans			
	No. of Clients	Amount	No. of Clients	Amount	No. of Clients	Amount	No. of Clients	Amount	No. of Clients	Amount
Clientele Spread										
Clients with one loan only	541	31,619	68.4	460	5,330	14.8	6,927	20,169	11.0	
Clients with two loans	84	9,673	20.9	331	12,078	33.5	2,423	24,257	13.2	
Clients with three loans	23	3,024	6.5	144	10,194	28.3	2,096	34,833	19.0	
Clients with more than three loans	9	1,940	4.2	132	8,435	23.4	2,294	104,434	56.8	
Total	657	46,256	100.0	1,067	36,037	100.0	13,740	183,693	100.0	

/a At the time of loan application to MIB.

AEP Projects Department
October 28, 1977

KOREA

MEDIUM INDUSTRY BANK

Summary of Guarantee Operations, 1974 - June 30, 1977
(In W million)

	<u>1974</u>		<u>1975</u>		<u>1976</u>		<u>1977</u> (Up to June 30)	
	No.	Amount	No.	Amount	No.	Amount	No.	Amount
<u>Guarantees Issued</u>								
Short-term	485	4,875	2,961	27,951	5,617	58,912	2,453	32,458
Long-term	715	6,673	827	7,948	4	111	-	-
<u>Total</u>	<u>1,200</u>	<u>11,548</u>	<u>3,788</u>	<u>35,899</u>	<u>5,621</u>	<u>59,023</u>	<u>2,453</u>	<u>32,458</u>
<u>Guarantees Redeemed</u>								
Short-term	-	5,797	2,720	25,050	5,422	58,939	2,573	32,177
Long-term	-	6,638	923	8,878	14	204	2	11
<u>Total</u>	<u>-</u>	<u>12,435</u>	<u>3,643</u>	<u>33,928</u>	<u>5,436</u>	<u>59,143</u>	<u>2,575</u>	<u>32,188</u>
<u>Guarantees Outstanding</u>								
Short-term	263	1,507	504	4,408	699	4,381	579	4,662
Long-term	118	1,060	22	130	12	37	10	26
<u>Total</u>	<u>381</u>	<u>2,567</u>	<u>526</u>	<u>4,538</u>	<u>711</u>	<u>4,418</u>	<u>589</u>	<u>4,688</u>
(of which in foreign exchange)		(1,517)		(3,452)		(2,751)		(3,124)
Advances on guarantees		428		442		64		89
Total guarantees affected		942		1,017		154		226
(as % of total outstanding guarantees)		37%		22%		3.5%		4.8%

AEP Projects Department
October 28, 1977

KOREA
MEDIUM INDUSTRY BANK

Subprojects Approved Under IBRD Loan No. 1175-KO as of June 30, 1977

Subborrower	Industry	Product line New/Exp.	At loan application		Total project cost		MFIs financing		Incremental annual sales (₩ million)	Incremental annual exports (US\$ '000)	Incremental employment
			Total assets (₩ million)	employment	Total cost (₩ million)	Fixed assets (₩ million)	Local (₩ million)	Foreign (US\$ '000)			
1. Naigae Textile Co.	Textile	New	85	-	153	116	-	192	235	464	16
2. Woo Kook Mail San Co., Ltd.	Textile	Exp.	520	174	214	152	20	276	319	864	50
3. I-gyong Electronic Co., Ltd.	Machinery	Exp.	318	61	108	86	-	152	154	-	17
4. Lim Yang Industrial Co., Ltd.	Textile	New	25	-	211	172	-	234	114	234	78
5. Han Dae Industrial Co., Ltd.	Textile	Exp.	330	78	127	107	-	210	102	402	70
6. Sawang Chemical Industry	Chemical	Exp.	113	15	97	24	-	37	177	-	4
7. Dong Shin Textile Co.	Textile	New	125	5	269	219	-	336	170	350	63
8. Jin Yang Textile Co.	Textile	New	81	2	210	166	-	239	128	263	82
9. Sung Nam Textile Co.	Textile	Exp.	209	25	48	42	1	86	143	12	12
10. Nam Sung Woollen Textile Co.	Textile	Exp.	274	160	378	283	30	312	964	1,387	37
11. Tai Dong Electronics Co.	Machinery	Exp.	421	136	206	103	-	206	34	1,386	155
12. Lava Industry Co., Ltd.	Textile	Exp.	250	15	264	102	75	204	1,323	1,508	155
13. Dong Kyo Textile Co.	Textile	Exp.	243	347	324	185	73	280	1,088	439	11
14. Shin Heung Woollen Textile Co.	Machinery	New	139	200	422	223	241	66	2,220	3,060	52
15. Seo Un Electronic Co., Ltd.	Textile	New	94	5	187	165	20	243	262	540	155
16. Poong Hyung Nuisan Ind. Co., Ltd.	Textile	New	79	5	141	131	-	243	152	282	66
17. Hoo Sung Chinares Co., Ltd.	Textile	Exp.	200	284	285	258	107	185	412	495	166
18. Kum Soong Fiber Industrial Co.	Textile	Exp.	564	131	166	125	34	210	735	521	72
20. Tongbuk Enterprise Co., Ltd.	Textile	Exp.	897	358	339	183	16	367	126	150	25
21. Kookje Knitting Co., Ltd.	Textile	New	66	7	127	73	-	80	688	710	25
22. Dong Hwa Textile Co., Ltd.	Textile	Exp.	75	26	79	73	-	148	22	132	16
23. Sam Hwa Textile Co., Ltd.	Textile	New	68	6	118	94	-	173	307	634	45
24. Kum Kang Trading Co., Ltd.	Textile	New	120	-	272	200	-	370	347	720	79
25. Dae Yang Textile Co.	Textile	Exp.	238	122	199	150	57	241	156	243	80
26. O Il Yook Textile Indus. Co., Ltd.	Textile	Exp.	610	197	252	142	-	279	683	1,051	29
27. Jin Heung Woollen Textile Co.	Textile	New	83	2	111	111	-	243	137	279	63
28. Hyup Sung Textile Co.	Textile	New	138	2	209	186	-	333	113	262	29
29. Jaell Fire Service Ind. Co., Ltd.	Others	Exp.	160	71	122	64	-	90	242	148	50
30. Shin Hyung Elec. Mfg. Co., Ltd.	Machinery	Exp.	518	345	94	54	-	85	720	-	28
31. Dong Sung Textile Co.	Textile	New	123	2	210	186	-	334	150	262	29
32. Dae Shin Knitting Ind. Co., Ltd.	Textile	Exp.	147	286	72	36	-	62	263	480	342
33. Dae Sung Textile Co.	Textile	Exp.	96	30	159	134	-	249	124	156	76
34. Dae Yang Rubber Ind. Co.	Chemical	Exp.	566	238	424	126	-	198	1,621	1,091	31
35. Dong Sung Textile Co.	Textile	Exp.	496	275	438	338	98	364	222	2,869	74
36. Tae Il Woollen Textile Co. Ltd.	Textile	Exp.	166	44	88	80	-	167	138	267	30
37. Sam yung Wool Text. Ind. Co., Ltd.	Textile	Exp.	1,943	196	931	207	525	417	1,397	2,102	22
38. Chang Yeong Textile Co.	Machinery	Exp.	388	910	276	76	136	127	664	316	37
39. Dai Yang Woollen Textile Co., Ltd.	Textile	Exp.	170	484	276	95	90	255	1,442	285	38
40. Kyeong Industrial Co., Ltd.	Textile	Exp.	157	83	177	145	-	253	182	182	26
41. Kyeong Printing & Packaging Mfg. Co., Ltd.	Textile	Exp.	238	963	240	178	3	321	279	574	26
42. Sam Yung Jung Pan Printing	Printing	Exp.	461	110	138	73	-	160	157	109	11
43. Sam Yung March Mfg. Co.	Chemical	Exp.	119	23	50	39	-	82	148	135	9
44. Dae Seong Ind. Co.	Machinery	Exp.	307	287	262	152	-	215	530	469	35
45. Dai Hwa Sangsa Co., Ltd.	Food	Exp.	240	160	131	49	40	48	175	174	10
46. Mee Hwa Textile Co.	Textile	Exp.	865	156	357	165	-	299	1,136	5,514	49
47. Dae Bo Textile Ind. Co.	Textile	Exp.	115	56	248	219	-	370	420	470	79
48. Samho Sangsa Co., Ltd.	Others	Exp.	153	130	397	378	-	479	403	750	118
49. BHA Diamond Ind. Co., Ltd.	Metal	Exp.	440	185	252	114	-	92	2,268	4,677	445
50. Nam Yeung Ind. Co., Ltd.	Textile	Exp.	129	21	73	19	-	36	123	-	7
51. Yoo An Textile Co., Ltd.	Textile	Exp.	635	78	618	420	330	147	1,318	3,574	432
52. Gillsung Textile Co., Ltd.	Textile	Exp.	140	166	265	255	112	233	265	550	193
53. Chilsung Textile Co., Ltd.	Textile	Exp.	708	193	114	37	-	182	201	810	3
54. Sung Han Hosiery Co.	Textile	Exp.	154	119	98	90	-	131	61	125	50
55. An Kwang Ind. Co., Ltd.	Textile	Exp.	235	121	170	141	13	230	342	370	10
56. Milyang Chinaware Co., Ltd.	Nonmetallic	Exp.	232	566	184	45	10	42	1,198	966	22
57. Il Shin Ind. Co.	Textile	Exp.	495	199	200	138	50	198	1,198	332	100
58. Bo Myong Co.	Rubber	New	30	-	64	62	-	40	261	513	21
59. Se Il Chem. Co. Ind. Co.	Chemical	Exp.	388	195	521	317	165	348	2,279	332	100
60. Yungdae Pharm. Co.	Textile	Exp.	1,218	412	165	178	-	304	1,491	1,193	104
61. Hyeon Textile Co.	Textile	Exp.	587	163	255	195	27	318	393	1,986	86
62. Sang An Textile Co.	Textile	Exp.	587	163	255	195	30	318	393	1,986	86
63. Poong Chin Products	Textile	New	25	25	45	41	-	41	165	299	18
64. Seoul Copy Co.	Services	Exp.	127	77	104	47	-	69	131	244	18
65. Kong Jak Hosiery Co.	Textile	Exp.	82	95	45	42	-	73	75	244	10
66. Shin Heung Dyeing & Finishing Co.	Textile	Exp.	296	169	95	69	-	150	316	461	15
67. Far East Sprinkler Co.	Metal	Exp.	163	58	48	24	-	36	562	-	31
57. Far East Sprinkler Co.	Metal	Exp.	313	40	82	54	11	82	60	-	20
58. Hankuk Metallizing Mould Co.	Metal	Exp.	313	40	82	54	11	82	60	-	20
59. Cosmic Electron	Machinery	Exp.	297	134	293	200	-	313	333	382	28

Subborrower	Industry	Product line New/Exp.	At loan application		Total project cost		MB's financing		Incremental annual sales (US\$ million)	Incremental annual exports (US\$ '000)	Incremental employment
			Total assets (₩ million)	Total employment	Total (₩ million)	Fixed assets (₩ million)	Local (₩ million)	Foreign (US\$ '000)			
70. Shin Hwa Ind. Co.	Machinery	Exp.	481	196	573	245	34	390	721	150	73
71. Soo Chang Ind. Co.	Textile	Exp.	138	22	35	31	3	48	78	58	10
72. Tae Lim Woolen Textile	Textile	Exp.	162	219	162	162	-	204	119	-	10
73. Dong Young Ind. Co.	Machinery	Exp.	254	160	206	72	30	167	32	40	24
74. Young Il Chem. Co.	Chemical	Exp.	82	28	68	178	-	131	151	300	8
75. Jeil Geared Motor Mfg.	Machinery	Exp.	283	212	212	178	-	252	28	121	51
76. Li Yang Pharm. Ind. Co.	Chemical	Exp.	2,173	189	957	113	-	174	607	198	39
77. Kam Kang Dies Co.	Metal	Exp.	40	64	81	44	21	31	96	198	23
78. Sam Sung Kuma Print. Co.	Printing	Exp.	122	98	122	72	46	154	277	30	13
79. Sang Chang Wool Textile Co.	Textile	Exp.	135	39	128	102	-	148	220	30	25
80. Dong Yang Metal Works Co.	Metal	Exp.	271	33	129	158	-	118	204	130	11
81. Da Yang Metal Ind. Co.	Metal	Exp.	80	159	152	119	36	176	200	59	8
82. So Bang Metal Ind. Co.	Textile	Exp.	66	73	152	119	-	140	120	210	13
83. Pungnam Ind. Co.	Textile	Exp.	384	110	205	165	-	176	169	210	13
84. Sam Ho Textile Co.	Textile	Exp.	224	232	98	90	-	136	169	514	37
85. Tae Sung Rubber Co.	Rubber	Exp.	350	162	111	73	-	125	115	238	17
86. Tae Lim Woolen Textiles	Textile	Exp.	160	217	154	90	31	227	78	200	44
87. Sam Yang Electron Co.	Machinery	Exp.	101	79	155	85	48	115	162	200	44
88. Hae Dong Industrial Co.	Textile	Exp.	146	65	84	89	20	98	56	50	9
89. Tae Il Woolen Textile Co., Ltd.	Textile	Exp.	146	76	91	84	-	175	213	381	2
90. Sam Shin Bong Jick Co., Ltd.	Textile	Exp.	225	72	147	70	92	71	491	416	19
91. Kirim & Co., Ltd.	Textile	New	18	18	114	103	-	110	332	827	32
92. Dong Bang Steel Mfg. Co., Ltd.	Basic metal	Exp.	234	173	344	283	16	416	563	-	35
93. Chunnam Motors Indust. Co.	Metal	Exp.	125	143	141	96	-	160	514	-	48
94. Shin Chang Co.	Machinery	Exp.	361	150	58	40	-	46	250	299	5
95. Dong Shin Textile Co.	Textile	Exp.	424	72	90	71	-	148	270	500	60
96. Shin Mha Mulsan Co., Ltd.	Metal	Exp.	358	184	138	83	-	107	210	140	6
97. Shin Chang Woolen Textile Co.	Textile	Exp.	90	72	72	66	-	135	202	78	32
98. Shin Heung Weaving Co.	Textile	Exp.	116	55	205	136	-	326	27	113	50
99. Song Nam Indust. Co., Ltd.	Machinery	Exp.	420	151	150	136	30	93	155	213	56
100. Jin Heung Textile Co.	Textile	New	103	1	168	-	-	254	226	433	34
101. Han Il Synthetic Printing	Printing	Exp.	93	43	63	39	20	65	208	167	15
102. Seon Il Metal Ind. Co.	Metal	Exp.	172	66	71	70	-	72	71	-	12
103. Nae Chang Agr. Prod. Co.	Food	Exp.	260	98	309	210	83	275	495	-	14
104. Koryol Ind. Co.	Textile	Exp.	182	12	85	-	20	121	75	69	12
105. Koo Chang Textile	Textile	New	180	1	84	-	-	139	71	-	13
106. Dae Hanung Machinery Co.	Machinery	Exp.	189	41	108	105	-	188	158	-	29
107. Dai Han Anchor Chain Mfg. Co., Ltd.	Metal	Exp.	558	123	37	23	20	36	291	413	7
108. Han Hung Wire Ind. Co.	Metal	Exp.	186	73	59	21	-	35	112	-	13
109. Asia Ind. Co.	Machinery	Exp.	347	96	169	164	25	279	384	-	82
110. Dae Il Textile Ind.	Textile	Exp.	64	43	41	21	-	33	273	187	22
111. Shin Jin Valve Ind. Co., Ltd.	Metal	Exp.	268	126	294	196	60	231	346	93	138
112. Sung Mha Industy Co.	Textile	Exp.	84	35	97	76	-	161	39	25	53
113. Yu Sung Metal Works	Metal	Exp.	505	122	277	220	29	347	442	-	36
114. Duk Heung Steel Co., Ltd.	Chemical	Exp.	492	26	81	29	-	42	128	-	20
115. Il Shin Chemical Co.	Chemical	Exp.	237	193	170	127	45	211	387	79	28
116. Dae Wang Ind. Co.	Textile	Exp.	172	39	81	46	10	75	184	-	17
117. Won Hap Machinery Co.	Machinery	Exp.	153	49	199	176	-	200	231	460	36
118. Mon Pyung Ind. Co.	Textile	New	87	3	163	-	-	241	253	1,509	23
119. Kun Kwang Wool Textile	Textile	Exp.	466	93	255	-	-	367	153	-	12
120. Dong Sung Machine Co.	Machinery	Exp.	294	62	291	284	-	488	193	-	-
121. Dong Shin Hydraulic Machinery Co.	Machinery	Exp.	201	81	188	140	19	245	246	-	29
122. Yoo Heung Electric Co., Ltd.	Machinery	New	21	3	87	82	-	108	80	115	29
123. Il Shin Metal Spinning Co., Ltd.	Textile	Exp.	72	44	249	220	-	293	54	-	24
124. Dong Hap Textile Co.	Textile	Exp.	130	103	230	50	24	337	79	-	28
125. Dae Il Industial Co.	Machinery	Exp.	324	185	63	-	-	85	209	400	12
126. Dae Il Industial Co.	Textile	Exp.	1,098	196	941	487	-	793	1,145	855	115
127. Sin Tae Yang Textile Ind. Co.	Textile	Exp.	254	196	272	214	-	344	94	157	132
128. Kwangyong Toppam Printing Co., Ltd.	Printing	Exp.	599	114	721	579	-	985	153	-	29
129. Jeil Machine Ind. Co.	Machinery	Exp.	227	110	978	769	384	400	1,960	-	231
130. Jung Young Ind. Co.	Metal	Exp.	541	216	136	86	51	100	907	-	3
131. Kwang-Ju Nae Seon Lathie Works	Machinery	Exp.	461	104	117	73	-	200	141	240	17
132. Dae Sung Chemical Co.	Chemical	Exp.	153	31	48	21	-	150	151	-	12
Total			40,959	16,294	28,136	17,191	3,533	26,929	51,265	60,639	6,665

MB Projects Department
October 28, 1977

KOREA

MEDIUM INDUSTRY BANK

Summarized Balance Sheets, 1974-June 30, 1977
(In W million)

As of December 31	1974	1975	1976	June 30, 1977
	-----	Audited	-----	Unaudited /a
ASSETS				
<u>Current Assets</u>				
Cash and bank deposits /b	39,152	65,507	83,409	85,327
Investment in securities	3,533	4,363	8,737	11,651
Interest receivable	2,485	3,199	2,921	-
Short-term working capital loans	63,832	85,226	124,510	146,266
Other current assets	1,542	572	1,279	2,505
<u>Total Current Assets</u>	<u>110,544</u>	<u>158,867</u>	<u>220,856</u>	<u>245,749</u>
<u>Term Portfolio</u>				
Working capital loans	44,979	47,444	33,400	37,426
Domestic currency equipment loans	22,490	26,306	33,429	36,038
Foreign currency loans	26,530	33,389	42,863	46,256
<u>Total Term Loans</u>	<u>93,999</u>	<u>107,139</u>	<u>109,692</u>	<u>119,720</u>
Less: Provisions	-	280	305	228
Net portfolio	93,999	106,859	109,387	119,492
Property and equipment (net)	2,601	3,005	3,407	4,252
<u>Other Assets</u>				
Long-term lease deposits	1,784	2,265	3,277	3,614
Properties acquired through foreclosure	1,198	1,036	1,515	728
Receivable from sale of foreclosed properties	4,304	3,686	3,767	3,919
<u>Total Other Assets</u>	<u>7,286</u>	<u>6,987</u>	<u>8,559</u>	<u>8,261</u>
<u>Total Assets</u>	<u>214,430</u>	<u>275,718</u>	<u>342,209</u>	<u>377,754</u>
LIABILITIES				
<u>Current Liabilities</u>				
Short-term deposits	71,343	95,570	138,751	168,651
Borrowings from BOK	10,253	19,615	22,050	15,251
Dividends payable	184	184	9	-
Taxes payable	50	59	150	-
Due to correspondent banks	3,047	7,960	8,372	8,545
Accrued interest and others	10,126	13,940	27,118	23,425
<u>Total Current Liabilities</u>	<u>95,003</u>	<u>137,328</u>	<u>196,450</u>	<u>215,872</u>
<u>Long-Term Liabilities</u>				
Savings deposits	57,863	69,181	64,151	72,039
Borrowings from GUK	15,520	13,452	10,842	11,204
Borrowings from NIF	1,627	5,128	8,523	10,124
Borrowings from IRF	10,403	8,634	6,131	5,074
Foreign currency borrowings	27,465	35,113	43,619	45,572
<u>Total Long-Term Liabilities</u>	<u>112,878</u>	<u>131,508</u>	<u>133,266</u>	<u>144,013</u>
<u>Total Liabilities</u>	<u>207,881</u>	<u>268,836</u>	<u>329,716</u>	<u>360,085</u>
EQUITY				
Paid-in share capital	3,060	3,060	8,060	13,060
Reserves	1,280	1,430	1,941	1,941
Retained earnings	2,209	2,392	2,492	2,868
<u>Total Equity</u>	<u>6,549</u>	<u>6,882</u>	<u>12,493</u>	<u>17,869</u>
<u>Total Liabilities and Equity</u>	<u>214,430</u>	<u>275,718</u>	<u>342,209</u>	<u>377,754</u>
<u>Outstanding Guarantees</u>				
Short-term guarantees	1,946	4,408	4,381	4,612
Long-term guarantees	621	130	37	76
<u>Total Guarantees</u>	<u>2,567</u>	<u>4,538</u>	<u>4,418</u>	<u>4,688</u>
<u>Ratios</u>				
Current ratio	1.2	1.2	1.1	1.1
Long-term debt/equity /c	15.8:1	17.4:1	9.8:1	7.4:1
Total debt/equity	31.8:1	39.1:1	26.4:1	20.1:1
Reserves and provisions as % of portfolio /d	2.2%	2.1%	2.0%	1.9%

/a In accordance with bank accounting practice in Korea, MIB keeps internal financial records on a modified cash basis, recognizing income on a cash basis and expenses on an accrual basis. The June 30, 1977 accounts were prepared on that basis and therefore underestimate net profits and retained earnings.

/b Including reserve requirements with BOK.

/c Including long-term guarantees and savings deposits net of BOK reserve requirements.

/d Total portfolio including guarantees.

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MEDIUM INDUSTRY BANK

Summarized Income Statements, 1974-June 30, 1977
(In W million)

Year ended December 31	1974	1975	1976	June 30, 1977
	-----	Audited	-----	Unaudited /a
<u>Income</u>				
Interest on loans	17,325	24,147	31,122	18,067
Interest on deposits & securities	2,435	3,568	3,383	1,977
Guarantee fees, commissions, etc.	1,077	1,476	1,900	1,127
Other income	643	512	499	221
<u>Total income</u>	<u>21,480</u>	<u>29,703</u>	<u>36,904</u>	<u>21,392</u>
<u>Expenses</u>				
Financial expenses	13,087	18,827	24,648	14,348
Administrative & general expenses	6,782	9,296	10,021	5,964
Provisions for doubtful accounts /b	77	280	630	-
Other expenses /c	859	724	929	704
<u>Total expenses</u>	<u>20,805</u>	<u>29,127</u>	<u>36,228</u>	<u>21,016</u>
Income before tax	675	576	676	376
Income tax	50	59	64	-
<u>Net income</u>	<u>625</u>	<u>517</u>	<u>612</u>	<u>376</u>
<u>Appropriation</u>				
Dividends	184	184	1	-
Reserves	105	150	512	-
Unappropriated retained earnings	336	183	99	-
<u>Total</u>	<u>625</u>	<u>517</u>	<u>612</u>	<u>-</u>
<u>Financial Performance</u>				
<u>Percentage of average total assets</u>				<u>6-month period</u>
1. Gross income	11.1	12.1	11.9	5.9
2. Financial expenses	6.7	7.7	8.0	4.0
3. Gross spread (1-2)	4.4	4.4	3.9	1.9
4. Administrative expenses	4.0	4.1	3.5	1.8
5. Provisions				-
6. Income tax	0.1	0.1	0.2	-
7. Net income	0.3	0.2	0.2	0.1
<u>Net profit as % of</u>				
Average equity	9.9	7.7	6.3	2.5
Share capital	20.4	16.9	7.6	2.9
<u>Other ratios</u>				
Income from loans as % of average loan portfolio	12.8	13.8	14.6	7.2
Cost of debt as % of average total borrowings	7.5	8.5	9.1	4.6
Interest spread	5.3	5.3	5.5	2.6
Cash dividends as % of par	6	6	-	-
Dividend payout ratio	29%	36%	0.2%	-
Book value as % of par	214	225	155	137
Interest cover ratio /d	1.07	1.06	1.06	1.03
Debt service cover /e	1.18	1.08	1.18	1.36
Return on average total assets /f	7.1%	7.9%	8.2%	4.1%

/a As indicated in footnote /a to Table 4.8, the accounts for the first 6 months of 1977 underestimate net income for that period. Care should be observed in interpreting the financial ratios derived from this 6-month operation.

/b Write offs in 1974 and 1976 amounted to W 77 million and W 605 million respectively.

/c Including losses on foreign exchange transactions.

/d Net earnings before tax, provisions, interest and depreciation to interest charges.

/e Net income + noncash charges + interest charges + term loan collections to interest charges + repayment of term borrowings (excluding collection of term working capital loans and repayments of savings deposits).

/f Net income before tax and interest to average total assets.

KOREA

MEDIUM INDUSTRY BANK

Summarized Cash Flow Statements, 1974-1976
(in W million)

	1974	1975	1976
<u>Sources</u>			
Operations:			
Net income	625	517	612
Non-cash charges	245	474	888
Subtotal	<u>870</u>	<u>991</u>	<u>1,500</u>
Issuance of shares for cash	-	-	5,000
Drawdown on:			
Foreign currency borrowings	11,788	10,253	13,504
Government borrowings	500	-	29
BOK	66,075	210,446	293,753
NIF	1,627	3,646	4,400
IRF	4,803	174	-
Subtotal	<u>84,793</u>	<u>224,519</u>	<u>311,686</u>
Collections:			
Foreign currency loans	2,199	3,647	4,303
Domestic currency equipment loans	4,032	4,184	11,632
Working capital loans	578,281	820,492	1,148,988
Subtotal	<u>584,512</u>	<u>828,323</u>	<u>1,164,923</u>
Increase in savings deposits	1,904	11,318	-5,030
Increase in short-term deposits	15,647	24,227	43,181
Increase in current liabilities /a	1,837	8,736	13,680
<u>Total sources</u>	<u>689,563</u>	<u>1,098,114</u>	<u>1,534,940</u>
<u>Uses</u>			
Additions to fixed assets (gross)	304	598	660
Disbursements:			
Foreign currency loans /b	11,726	10,506	13,777
Domestic currency equipment loans	9,310	8,000	18,755
Working capital loans /c	609,209	844,351	1,174,228
Subtotal	<u>630,245</u>	<u>862,857</u>	<u>1,206,760</u>
Repayment of borrowings:			
Foreign currency borrowings	1,742	2,605	4,998
BOK	60,213	201,083	291,318
Government of Korea	1,531	2,068	2,639
NIF	-	146	1,004
IRF	682	1,943	2,503
Subtotal	<u>64,168</u>	<u>207,845</u>	<u>302,462</u>
Increase in current assets (receivables and others)	555	-256	429
Increase in short-term investments (securities)	-6,969	830	4,374
Increase in cash	1,537	26,355	17,902
Subtotal	<u>-4,877</u>	<u>26,929</u>	<u>22,705</u>
Increase in other assets /d	-539	-299	1,572
Write offs	77	-	605
Dividend payment	185	184	176
<u>Total uses</u>	<u>689,563</u>	<u>1,098,114</u>	<u>1,534,940</u>

/a Taxes payable, due to correspondent banks, accrued interest.

/b Inclusive of W 56 million disbursed in 1976 from KFX.

/c Inclusive of W 1,540 million disbursed in 1976 from KFX.

/d Lease deposits + receivables from foreclosures and properties acquired through foreclosure.

KOREA

MEDIUM INDUSTRY BANK

Status of Loan Portfolio as of June 30, 1977
(In W million)

	Total Outstanding Loans		Interest	Principal	Arrears			Principal affected by arrears		
					Total	As % of		Amount	As % of	
	Amount	%				Total arrears	Total out- standing loans /c		Total affected loans	Total outstanding /c
<u>Equipment Loans</u>										
Projects under implementation	4,258	5.2	39	72	111	5.2	2.6	236	2.5	5.5
Projects in initial stage of operation /a	15,348	18.7	24	56	80	3.8	0.5	815	8.7	5.3
Projects in operation /b	62,687	76.1	686	1,256	1,942	91.0	3.1	8,293	88.8	13.2
of which:										
with operational problems	(8,293)	(10.1)	-	-	-	-	-	-	-	-
problem free	(54,394)	(66.0)	-	-	-	-	-	-	-	-
<u>Total</u>	<u>82,293</u>	<u>100.0</u>	<u>749</u>	<u>1,384</u>	<u>2,133</u>	<u>100.0</u>	<u>2.6</u>	<u>9,344</u>	<u>100.0</u>	<u>11.4</u>
<u>Working Capital Loans</u>										
Projects under implementation	-	-	-	-	-	-	-	-	-	-
Projects in initial stage of operation /a	9,919	5.4	32	157	189	2.7	1.9	257	5.0	2.6
Projects in operation /b	173,774	94.6	1,828	5,031	6,859	97.3	3.9	4,931	95.0	2.8
of which:										
with operational problems	(4,931)	(2.7)	-	-	-	-	-	-	-	-
problem free	(168,843)	(91.9)	-	-	-	-	-	-	-	-
<u>Total</u>	<u>183,693</u>	<u>100.0</u>	<u>1,860</u>	<u>5,188</u>	<u>7,048</u>	<u>100.0</u>	<u>3.8</u>	<u>5,188</u>	<u>100.0</u>	<u>2.8</u>
<u>Total Loans</u>										
Projects under implementation	4,258	1.6	39	72	111	1.2	2.6	236	1.6	5.5
Projects in initial stage of operation /a	25,267	9.5	56	213	269	2.9	1.1	1,072	7.4	4.2
Projects in operation /b	236,461	88.9	2,514	6,287	8,801	95.9	3.7	13,224	91.0	5.6
of which:										
with operational problems	(13,224)	(5.0)	-	-	-	-	-	-	-	-
problem free	(223,237)	(83.9)	-	-	-	-	-	-	-	-
<u>Total</u>	<u>265,986</u>	<u>100.0</u>	<u>2,609</u>	<u>6,572</u>	<u>9,181</u>	<u>100.0</u>	<u>3.5</u>	<u>14,532</u>	<u>100.0</u>	<u>5.5</u>

/a Projects which have not yet completed their first year of operation.

/b Projects which have been operating for more than one year.

/c Under each category.

AEF Projects Department
October 28, 1977

KOREA

MEDIUM INDUSTRY BANK

Analysis of Loans in Arrears as of June 30, 1977
(In W million)

Nature of Arrears	Domestic currency			Equipment loans			Total			Working capital loans			Total		
	Amount in arrears	Principal affected Amount	%	Amount in Arrears	Principal affected Amount	%	Amount in arrears	Principal affected Amount	%	Amount in arrears	Principal affected Amount	%	Amount in arrears	Principal affected Amount	%
Principal	1,173			211			1,384			5,188			6,572		
Interest	409			340			749			1,860			2,609		
Total	1,582	6,306	17.5/a	551	3,038	6.6/a	2,133	9,344	11.4/a	7,048	5,188	2.8/a	9,181	14,532	5.5/a
Age Distribution															
Less than 3 months	956	5,815	92.2	165	2,727	89.7	1,121	8,542	91.5	2,535	2,314	44.6	3,656	10,856	74.7
3 to 6 months	251	224	3.6	5	75	2.5	256	299	3.2	1,295	1,087	21.0	1,551	1,386	9.5
6 to 12 months	154	129	2.0	-	12	0.4	154	141	1.5	941	681	13.1	1,095	822	5.7
12 to 24 months	81	60	1.0	39	36	1.2	120	96	1.0	448	254	4.9	568	350	2.4
24 months and over	140	78	1.2	342	188	6.2	482	266	2.8	1,829	852	16.4	2,311	1,118	7.7
Total	1,582	6,306	100.0	551	3,038	100.0	2,133	9,344	100.0	7,048	5,188	100.0	9,181	14,532	100.0
Sectoral Distribution															
Manufacturing:															
Food, beverage, tobacco	29	136	2.2	14	327	10.8	43	463	4.9	502	426	8.2	545	889	6.1
Textile, wearing apparel, leather	592	2,681	42.6	301	2,319	76.3	893	5,000	53.5	2,874	2,330	45.0	3,767	7,330	50.5
Wood and wood products	214	733	11.6	-	-	-	214	733	7.8	578	386	7.4	792	1,119	7.7
Paper, paper products, printing	98	329	5.2	18	143	4.7	116	472	5.1	805	515	9.9	921	987	6.8
Chemicals, rubber, plastics	83	278	4.4	31	38	1.3	114	316	3.4	533	327	6.3	647	643	4.4
Nonmetallic mineral products	43	103	1.6	-	-	-	43	103	1.1	524	386	7.4	567	489	3.4
Basic metals	-	-	-	-	-	-	-	-	-	673	403	7.8	673	403	2.8
Metal products, machinery, equipment	184	978	15.5	27	16	0.5	211	994	10.6	11	7	0.1	222	1,001	6.9
Others	214	870	13.8	105	154	5.1	319	1,024	11.0	24	15	0.3	343	1,039	7.1
Subtotal	1,457	6,108	96.9	496	2,997	98.7	1,953	9,105	97.4	6,524	4,795	92.4	8,477	13,900	95.7
Nonmanufacturing:															
Construction	121	183	2.9	11	20	0.6	132	203	2.2	5	5	0.1	137	208	1.4
Transportation	4	15	0.2	44	21	0.7	48	36	0.4	188	148	2.9	236	184	1.3
Services and commerce	-	-	-	-	-	-	-	-	-	141	105	2.0	141	105	0.7
Mining	-	-	-	-	-	-	-	-	-	131	93	1.8	131	93	0.6
Others	-	-	-	-	-	-	-	-	-	59	42	0.8	59	42	0.3
Subtotal	125	198	3.1	55	41	1.3	180	239	2.6	524	393	7.6	704	632	4.3
Total	1,582	6,306	100.0	551	3,038	100.0	2,133	9,344	100.0	7,048	5,188	100.0	9,181	14,532	100.0

/a As % of portfolio within each category.

AEP Projects Department
October 28, 1977

KOREA

MEDIUM INDUSTRY BANK

Collection Performance During the Period 1974 - June 30, 1977
(In W million)

	Total due during the year												
	Overdues		Maturing during the year		Total due during the year			Actual collections			Collection ratio		
Principal	Interest	Principal	Interest	Principal	Interest	Total	Principal	Interest	Total	Principal	Interest	Total	
A. Collection Ratios													
Domestic currency equipment loans													
1974	255	153	4,218	2,197	4,473	2,350	6,823	4,032	2,233	6,265	90.1	95.0	91.8
1975	441	117	4,349	3,014	4,790	3,131	7,921	4,184	2,943	7,127	87.4	94.0	90.0
1976	606	188	11,605	4,098	12,211	4,286	16,497	11,632	4,023	15,655	95.3	93.9	94.9
1977 (Jan.-June)	579	263	10,115	2,230	10,694	2,493	13,187	9,521	2,084	11,605	89.0	83.6	88.0
Foreign currency equipment loans													
1974	116	210	2,241	1,902	2,357	2,112	4,469	2,199	1,980	4,179	93.3	93.8	93.5
1975	158	132	3,766	2,591	3,924	2,723	6,647	3,647	2,560	6,207	92.9	94.0	93.4
1976	277	163	4,415	3,667	4,692	3,830	8,522	4,303	3,636	7,939	91.7	94.9	93.2
1977 (Jan.-June)	389	194	2,822	2,011	3,211	2,205	5,416	3,000	1,865	4,865	93.4	84.6	89.8
Working capital loans													
1974	2,741	1,161	578,829	13,579	581,570	14,740	596,310	578,281	13,373	591,654	99.4	90.7	99.2
1975	3,289	1,367	821,267	17,903	824,556	19,270	843,826	820,492	17,597	838,089	99.5	91.3	99.3
1976	4,064	1,673	1,149,070	23,862	1,153,134	25,535	1,178,669	1,148,988	24,125	1,173,113	99.6	94.5	99.5
1977 (Jan.-June)	4,146	1,410	668,875	14,887	673,021	16,297	689,318	667,833	14,437	682,270	99.2	88.6	99.0
Total													
1974	3,112	1,524	585,288	17,678	588,400	19,202	607,602	584,512	17,586	602,098	99.3	91.6	99.1
1975	3,888	1,616	829,382	23,508	833,270	25,124	858,394	828,323	23,100	851,423	99.4	91.9	99.2
1976	4,947	2,024	1,165,090	31,627	1,170,037	33,651	1,203,688	1,164,923	31,784	1,196,707	99.6	94.5	99.4
1977 (Jan.-June)	5,114	1,867	681,812	19,128	686,926	20,995	707,921	680,354	18,386	698,740	99.0	87.6	98.7
B. Status of Loan Portfolio (in W million)													
Year Ending December 31,			1974		1975		1976		June 30, 1977				
			Amount	%	Amount	%	Amount	%	Amount	%			
Principal outstanding			157,831	100.0	190,673	100.0	232,600	100.0	265,986	100.0			
Of which:													
In grace period /a			27,525	17.5	25,668	13.5	31,048	13.4	35,020	13.2			
Repaying regularly			123,287	78.1	156,356	82.0	194,329	83.5	216,434	81.3			
In arrears			7,019	4.4	8,649	4.5	7,223	3.1	14,532	5.5			
(over 3 months)			(5,054)	(3.2)	(5,705)	(3.0)	(4,889)	(2.1)	(3,676)	(1.4)			

/a All working capital loans are considered as having no grace period.

KOREA

MEDIUM INDUSTRY BANK

Long-Term Borrowings as of June 30, 1977
(In W million)

	Loan amount /a	Approvals	Commit- ments	Disburse- ments	Repayments	Out- standing	Interest rate		Maximum term (yrs)		Date of loan agreement
							Borrowing	Relending	For MIB	For subborrowers	
I. <u>Foreign Currency Borrowings</u>											
USAID	3,404	3,404	3,404	3,404	2,433	971	5.0	8.0	15	15	1966-67
OECD: 1st loan	7,187	7,187	7,187	7,187	4,422	2,765	7.0	8.0	13	13	1966
2nd loan	3,596	3,596	3,596	3,596	1,664	1,932	7.0	8.0	13	13	1967
Subtotal	<u>10,783</u>	<u>10,783</u>	<u>10,783</u>	<u>10,783</u>	<u>6,086</u>	<u>4,697</u>					
KFW: 1st loan	3,040	3,040	3,040	3,040	3,040	-	5.0	8.0	6	6	1965
2nd loan	1,621	1,617	1,584	1,465	11	1,454	7.0	9.0	30	15	1973
Subtotal	<u>4,661</u>	<u>4,657</u>	<u>4,624</u>	<u>4,505</u>	<u>3,051</u>	<u>1,454</u>					
ADB: 1st loan	4,830	4,830	4,830	4,830	1,836	2,994	6.875	10.0	15	15	1969
2nd loan	7,264	7,264	7,264	7,264	1,450	5,814	7.5 to 8.75	9.5 to 10.75	15	15	1971
3rd loan	14,550	14,475	14,475	13,906	653	13,253	7.5 to 8.75	9.5 to 10.75	15	15	1973
4th loan	14,550	6,027	214	-	-	-	8.9	10.9	15	15	1976
Subtotal	<u>41,194</u>	<u>32,596</u>	<u>26,783</u>	<u>26,000</u>	<u>3,939</u>	<u>22,061</u>					
Exim Bank of Japan	8,728	8,728	8,728	8,728	3,122	5,606	6.25	8.25	13	13	1971
IBRD: 1st loan	14,550	13,061	12,300	8,780	16	8,764	8.5	10.5	15	15	1975
Government syndicated borrowings /b	808	808	808	808	-	808	LIBOR + 1 7/8%	LIBOR + 2%	5	5	1976
Korea foreign exchange /c	2,425	394	394	394	-	394	LIBOR + 1.5%	LIBOR + 2%	8	8	1977
Total foreign currency borrowings	<u>86,553</u>	<u>74,431</u>	<u>67,824</u>	<u>63,402</u>	<u>18,647</u>	<u>44,755</u>					
II. <u>Domestic Currency</u>											
Government of Korea						2,526	2.0		25		1963-75
Counterpart funds						8,532	11 to 15%	13 to 17%	10	3 & 8/d	1962-74
Special account						146	11 to 15%		5		1965-71
Subtotal						<u>11,204</u>					
National Investment Fund						10,124	11.5	13 to 15	3 & 8/d	3 & 8/d	
Industrial Rationali- zation Fund						5,074	11.5	13 to 15	3 & 8/d	3 & 8/d	
Deposits (over one-year maturity)						72,039	12.2 to 16.2	17 to 18	1 to 6	1 to 6	
Total domestic currency borrowings						<u>98,441</u>					

/a Net of cancellations.

/b Represents part of a US\$6 million loan made available by the Korean Government to MIB in 1976 and which was utilized to the tune of US\$4.3 million for financing imports of raw materials and US\$1.7 million for equipment financing.

/c US\$5 million loan made available by the Government of Korea from the country's foreign exchange reserves. Referred to in the report as KFX.

/d Three years for working capital loans and eight years for equipment loans.

KOREA
MEDIUM INDUSTRY BANK

Net Resource Position as of December 31, 1976 and June 30, 1977
(In W million)

	As of Dec. 31, 1976	As of June 30, 1977
I. Domestic Currency		
A. Long-term		
Equity: Paid-in capital	8,060	13,060
Reserves and retained earnings	4,433	4,809
<u>Total equity</u>	<u>12,493</u>	<u>17,869</u>
Borrowings from Government	10,842	11,204
Borrowings from NIF and IRF	14,654	15,198
Savings deposits (over one year)	64,151	72,039
<u>Total long-term domestic currency resources</u>	<u>102,140</u>	<u>116,310</u>
Less: Domestic currency outstanding term loans	66,829	73,464
Investment in fixed assets (net)	3,407	4,252
Other long-term assets /a	8,559	8,261
BOK's reserve requirement against term deposits	10,906	12,246
Subtotal	<u>89,701</u>	<u>98,223</u>
Resources available for further disbursement	12,439	18,087
Less: Undisbursed commitments	-	-
Resources available for further commitment	12,439	18,087
B. Short-term		
Demand and savings deposits (less than one year)	138,751	168,651
Short-term borrowings from BOK	22,050	15,251
<u>Total short-term domestic currency resources</u>	<u>160,801</u>	<u>183,902</u>
Less: Short-term loans outstanding	124,510	146,266
BOK's reserve requirement against deposits	28,011	32,845
Subtotal	<u>152,521</u>	<u>179,111</u>
Resources available for further commitment	8,280	4,791
C. Total domestic currency resources		
Total long-term resources	102,140	116,310
Total short-term resources	160,801	183,902
<u>Total resources</u>	<u>262,941</u>	<u>300,212</u>
Less: Outstanding loans	191,339	219,730
Investment in property and equipment	3,407	4,252
BOK's reserve requirement	38,917	45,091
Other long-term assets	8,559	8,261
Subtotal	<u>242,222</u>	<u>277,334</u>
Resources available for further disbursement	20,719	22,878
Less: Undisbursed loan commitments	-	-
Resources available for further commitment	20,719	22,878
II. Foreign Currency		
Total foreign currency resources	83,330	86,553
Less: Foreign currency loans disbursed	56,819	63,402
Resources available for further disbursement	26,511	23,151
Less: Undisbursed loan commitments	6,430	4,422
Net resources available for further commitments	20,081	18,729
Less: Uncommitted approvals	1,066	6,607
Net resources available for approvals	19,015	12,122

/a Long-term lease deposits, properties acquired through foreclosures and receivables from the sale of such properties.

KOREA
MEDIUM INDUSTRY BANK

Projected Operations, 1977-1981
(In W million)

	<u>1976</u> (Actual)	<u>1977</u>	<u>1978</u>	<u>1979</u>	<u>1980</u>	<u>1981</u>
<u>Approvals</u>						
Equipment loans						
In domestic currency /a	18,755	25,146	32,020	40,153	50,253	63,000
In foreign currency	13,533	17,735	21,340	25,705	30,798	36,375
Total equipment loans	<u>32,288</u>	<u>42,881</u>	<u>53,360</u>	<u>65,858</u>	<u>81,051</u>	<u>99,375</u>
Working capital loans /b (net increase)	25,240	39,166	51,483	68,480	75,054	95,883
Total approvals	<u>57,528</u>	<u>82,047</u>	<u>104,843</u>	<u>134,338</u>	<u>156,105</u>	<u>195,258</u>
<u>Commitments</u>						
Equipment loans						
In domestic currency	18,755	25,146	32,020	40,153	50,253	63,000
In foreign currency	13,589	17,468	21,460	26,093	29,924	36,132
Total equipment loans	<u>32,344</u>	<u>42,614</u>	<u>53,480</u>	<u>66,246</u>	<u>80,177</u>	<u>99,132</u>
Working capital loans (net increase)	25,240	39,166	51,483	68,480	75,054	95,883
Total commitments	<u>57,584</u>	<u>80,780</u>	<u>104,963</u>	<u>134,726</u>	<u>155,231</u>	<u>195,015</u>
<u>Disbursements</u>						
Equipment loans						
In domestic currency	18,755	25,090	32,020	40,153	50,253	63,000
In foreign currency	13,777	14,015	20,098	26,287	29,391	34,774
Total equipment loans	<u>32,532</u>	<u>39,105</u>	<u>52,118</u>	<u>66,440</u>	<u>79,644</u>	<u>97,774</u>
Working capital loans /b (net increase)	25,240	39,166	51,483	68,480	75,054	95,883
Total disbursements	<u>57,772</u>	<u>78,271</u>	<u>103,601</u>	<u>134,920</u>	<u>154,698</u>	<u>193,657</u>

/a No time lag is assumed between approval, commitment and disbursement of domestic currency loans since MIB enters into loan agreement with the borrowers immediately after approval of a loan and credits the borrower's account as soon as loan documents are signed.

/b On a gross basis, working capital loans are projected as follows:

	<u>1977</u>	<u>1978</u>	<u>1979</u>	<u>1980</u>	<u>1981</u>
Disbursements during the year	1,577,816	2,002,203	2,546,390	3,178,104	3,942,973
Less: collections during the year	1,538,650	1,950,720	2,477,910	3,103,050	3,847,090
Net increase	<u>39,166</u>	<u>51,483</u>	<u>68,480</u>	<u>75,054</u>	<u>95,883</u>

KOREA

MEDIUM INDUSTRY BANK

Projected Income Statements, 1977-81
(in W million)

	Actual 1976	Projected				
		1977	1978	1979	1980	1981
<u>Income</u>						
Interest on loans	31,122	41,045	51,355	65,805	83,038	103,473
Interest on deposits and securities	3,383	2,507	3,362	4,330	5,537	7,102
Guarantee fees, commissions, etc.	1,900	2,406	3,033	3,884	4,822	5,992
Other income	499	629	799	1,023	1,269	1,574
<u>Total income</u>	<u>36,904</u>	<u>46,587</u>	<u>58,549</u>	<u>75,042</u>	<u>94,666</u>	<u>118,141</u>
<u>Expenses</u>						
Financial expenses	24,648	31,561	39,264	48,706	60,505	74,987
Administrative and general expenses	10,021	12,626	16,035	20,525	25,451	31,559
Provisions for doubtful accounts	630	384	488	625	775	961
Other expenses	929	1,171	1,487	1,903	2,360	2,926
<u>Total expenses</u>	<u>36,228</u>	<u>45,742</u>	<u>57,274</u>	<u>71,759</u>	<u>89,091</u>	<u>110,433</u>
Income before tax	676	845	1,275	3,283	5,575	7,708
Income tax	64	68	102	263	446	617
<u>Net income</u>	<u>612</u>	<u>777</u>	<u>1,173</u>	<u>3,020</u>	<u>5,129</u>	<u>7,091</u>
<u>Appropriation</u>						
Dividends	1	316	497	1,251	1,500	1,500
Reserves	512	460	670	1,760	3,620	5,590
Unappropriated retained earnings	99	1	6	9	9	1
<u>Total</u>	<u>612</u>	<u>777</u>	<u>1,173</u>	<u>3,020</u>	<u>5,129</u>	<u>7,091</u>
<u>Financial Performance</u>						
<u>Percentage of Average Total Assets</u>						
1. Gross income	11.9	12.1	12.1	12.2	12.3	12.4
2. Financial expenses	8.0	8.2	8.1	7.9	7.9	7.9
3. Gross spread (1-2)	3.9	3.9	4.0	4.3	4.4	4.5
4. Administrative expenses	3.5	3.6	3.6	3.7	3.6	3.6
5. Provisions	0.2	0.1	0.1	0.1	0.1	0.1
6. Income tax	-	-	-	-	-	-
7. Net income	0.2	0.2	0.3	0.5	0.7	0.7
<u>Net Profit as % of</u>						
Average equity	6.3	5.1	5.4	9.6	13.1	16.2
Share capital	7.6	5.9	5.8	10.1	17.1	23.6
<u>Other Ratios</u>						
Income from loans as % of average loan portfolio	14.6	15.5	15.4	15.4	15.5	15.5
Cost of debt as % of average total borrowings	9.1	9.5	9.4	9.3	9.2	9.1
Interest spread	5.5	6.0	6.0	6.1	6.3	6.4
Cash dividends as % of par	-	3.0	3.0	5.0	5.0	5.0
Dividend pay-out ratio	0.2	41.0	42.0	41.0	29.0	21.0
Book value as % of par	155.0	137.0	128.0	124.0	137.0	155.0
Interest cover ratio /a	1.06	1.05	1.05	1.09	1.11	1.12
Debt service cover /b	1.18	1.20	1.29	1.38	1.41	1.44
Return on average total assets /c	8.2	8.4	8.4	8.5	8.6	8.7

/a Net earnings before tax, noncash charges and interest to interest charges.

/b Net income after tax + noncash charges + interest charges + term loan collections to interest charges + repayment of term borrowings (excluding collection of medium-term working capital loans and repayments of savings deposits).

/c Net income before tax and interest to average total assets.

KOREA

MEDIUM INDUSTRY BANK

Projected Balance Sheets 1977-1981
(In W million)

As of December 31,	1976 (Actual)	1977	1978	1979	1980	1981
ASSETS						
Current Assets						
Cash & bank deposits	83,409	99,056	117,872	142,958	175,952	212,337
Investment in securities	8,737	15,937	22,677	31,157	41,297	53,397
Interest receivable	2,921	3,680	4,674	5,983	7,419	9,200
Short-term working capital loans	124,510	158,370	200,580	255,410	315,560	392,310
Other current assets	1,279	1,664	2,081	2,624	3,259	4,029
Total current assets	220,856	278,707	347,884	438,132	543,487	671,273
Term Portfolio						
Working capital loans	33,400	38,706	47,979	61,629	76,533	95,666
Domestic currency equipment loans	33,429	45,148	59,087	75,583	95,581	120,326
Foreign currency loans	42,863	51,878	66,384	86,278	107,595	132,526
Total term loans	109,692	135,732	173,450	223,490	279,709	348,518
Less: provisions	305	384	488	625	775	961
Net portfolio	109,387	135,348	172,962	222,865	278,934	347,557
Property and equipment (net)	3,407	5,833	8,229	10,605	12,960	15,292
Other Assets						
Long-term lease deposits	3,277	3,605	3,970	4,370	4,810	5,290
Properties acquired through foreclosure	1,515	1,760	2,240	2,870	3,570	4,450
Receivable from sale of fore-closed properties	3,767	4,400	5,600	7,170	8,920	11,120
Total other assets	8,559	9,765	11,810	14,410	17,300	20,860
TOTAL ASSETS	342,209	429,653	540,885	686,012	852,681	1,054,982
LIABILITIES						
Current Liabilities						
Short-term deposits	138,751	167,950	197,903	221,574	261,319	307,540
Borrowings from BOK	22,050	32,250	45,510	62,748	85,157	114,288
Dividends payable	9	316	497	1,251	1,500	1,500
Taxes payable	150	68	102	263	446	617
Due to correspondent banks	8,372	8,790	9,230	9,690	10,170	10,680
Accrued interest & others	27,118	33,402	41,575	52,198	66,007	77,797
Total current liabilities	196,450	242,776	294,817	347,724	424,599	512,422
Long-term liabilities						
Savings deposits	64,151	87,952	119,407	171,886	226,571	297,440
Borrowings from GOK	10,842	10,742	10,750	12,508	15,231	19,218
Borrowings from NIF	8,523	13,246	19,846	27,326	35,866	45,766
Borrowings from IRF	6,131	4,349	3,295	2,195	1,095	295
Foreign currency borrowings	43,619	52,634	67,140	87,034	108,351	133,282
Total long-term liabilities	133,266	168,923	220,438	300,949	387,114	496,001
EQUITY						
Paid-in share capital	8,060	13,060	20,060	30,000	30,000	30,000
Reserves	1,941	2,401	3,071	4,831	8,451	14,041
Retained earnings	2,492	2,493	2,499	2,508	2,517	2,518
Total equity	12,493	17,954	25,630	37,339	40,968	46,559
TOTAL LIABILITIES & EQUITY	342,209	429,653	540,885	686,012	852,681	1,054,982
Outstanding guarantees						
Short-term guarantees	4,381	5,686	7,391	9,609	12,492	16,238
Long-term guarantees	37	57	75	97	126	165
Total guarantees	4,418	5,743	7,466	9,706	12,618	16,404
Ratios						
Current ratio	1.12	1.15	1.18	1.26	1.28	1.31
Long-term debt/equity /a	9.8:1	8.6:1	7.8:1	7.3:1	8.5:1	9.6:1
Total debt/equity	26.4:1	22.9:1	20.1:1	17.4:1	19.8:1	21.7:1
Reserves & provisions as % of portfolio /b	2.0	1.8	1.6	1.6	1.9	2.3

/a Excluding reserve requirements with BOK.

/b Total portfolio including guarantees.

AEP Projects Department
October 28, 1977

KOREA

MEDIUM INDUSTRY BANK

Projected Cash Flow Statements, 1977-81
(In W million)

	1977	1978	1979	1980	1981
<u>Sources</u>					
Operations					
Net income	777	1,173	3,020	5,129	7,091
Noncash charges	658	792	949	1,120	1,329
Subtotal	<u>1,435</u>	<u>1,965</u>	<u>3,969</u>	<u>6,249</u>	<u>8,420</u>
Issuance of shares for cash	5,000	7,000	9,940	-	-
Drawdown on					
(i) Foreign currency borrowings	14,015	20,098	26,287	29,391	34,774
(ii) Government borrowings	2,000	2,500	3,120	3,900	4,870
(iii) BOK	355,270	500,220	688,638	933,589	1,252,011
(iv) NIF	7,000	8,400	10,080	12,100	14,530
Subtotal	<u>378,285</u>	<u>531,218</u>	<u>728,125</u>	<u>978,980</u>	<u>1,306,185</u>
Collections					
Foreign currency loans	5,000	5,592	6,393	8,074	9,843
Domestic currency eqpt loans	13,371	18,081	23,657	30,255	38,255
Working capital loans	1,538,650	1,950,720	2,477,910	3,103,050	3,847,090
Subtotal	<u>1,557,021</u>	<u>1,974,393</u>	<u>2,507,960</u>	<u>3,141,379</u>	<u>3,895,188</u>
Increase in savings deposits	23,801	31,455	52,479	54,681	70,869
Increase in short-term deposits	29,199	29,953	23,671	39,745	46,221
Increase in current liabilities /a	6,620	8,647	11,244	14,472	12,471
<u>Total sources</u>	<u>2,001,361</u>	<u>2,584,631</u>	<u>3,337,388</u>	<u>3,235,510</u>	<u>5,339,354</u>
<u>Uses</u>					
Additions to fixed assets (gross)	2,700	2,700	2,700	2,700	2,700
Disbursements					
(i) Foreign currency loans	14,015	20,098	26,287	29,391	34,774
(ii) Domestic currency eqpt loans	25,090	32,020	40,153	50,253	63,000
(iii) Working capital loans	1,577,816	2,002,203	2,546,390	3,178,104	3,942,973
Subtotal	<u>1,616,921</u>	<u>2,054,321</u>	<u>2,612,830</u>	<u>3,257,748</u>	<u>4,040,747</u>
Repayments of borrowings					
(i) Foreign currency borrowings	5,000	5,592	6,393	8,074	9,843
(ii) GOK	2,100	2,492	1,362	1,177	883
(iii) BOK	345,070	486,960	671,400	911,180	1,222,880
(iv) NIF	2,277	1,800	2,600	3,560	4,630
(v) IRF	1,782	1,054	1,100	1,100	800
Subtotal	<u>356,229</u>	<u>497,898</u>	<u>682,855</u>	<u>925,091</u>	<u>1,239,036</u>
Increase in current assets /b	1,144	1,411	1,852	2,071	2,551
Increase in short-term investments /c	7,200	6,740	8,480	10,140	12,100
Increase in cash	15,647	18,816	25,086	32,994	36,385
Subtotal	<u>23,991</u>	<u>26,967</u>	<u>35,418</u>	<u>45,205</u>	<u>51,036</u>
Increase in other assets /d	1,206	2,045	2,600	2,890	3,560
Write offs	305	384	488	625	775
Dividend payments	9	316	497	1,251	1,500
<u>Total uses</u>	<u>2,001,361</u>	<u>2,584,631</u>	<u>3,337,388</u>	<u>3,235,510</u>	<u>5,339,354</u>

/a Taxes payable, due to correspondent banks, accrued interest.

/b Receivables and others.

/c Securities.

/d Lease deposits + receivables from foreclosures and properties acquired through foreclosure.

KOREAMEDIUM INDUSTRY BANKPolicy Statement

(Adopted by Board of Policy on November 13, 1969
and Amended on May 30, 1974)

I. Economic Role

MIB shall assist in the economic development of Korea in conformity with its purposes as stated in the Medium Industry Bank Act and By-Laws and in accordance with the Government's plans, policies and priorities. In order to accomplish this objective, MIB will promote the development of privately controlled medium and small enterprises (as defined from time to time by the Government of the Republic of Korea) in the country by (i) providing various types of financial assistance to them in the form of short-term credits for working capital purposes, medium- and long-term loans, equity participation, guarantees and underwritings; (ii) providing technical and managerial consulting services; and (iii) undertaking promotional activities in the identification and development of new projects. The term "privately-controlled" enterprises will be taken to mean enterprises which are privately operated and managed and in which the controlling interest is held by private investors. The mere fact that such enterprises have secured loans from government financial institutions, or that the Government holds a minority equity position will not exclude such enterprises from receiving financial assistance from MIB.

II. Development Policies

In extending its assistance MIB shall give preference to enterprises which will effectively contribute to broadening the base of the national economy and improving the balance of payments. Priority will be given to:

- (a) Export industries as designated by the Government.
- (b) Import-substitution industries and industries producing raw materials necessary for export and import-substitution industries.
- (c) Specialized industries or industries ancillary to large firms and machinery industries.
- (d) Industries with potential for exports or import-substitution.
- (e) Industries which will develop new products.
- (f) Indigenous industries and industries which make use of labor intensive technologies.

III. General Policies and Procedures

- (a) MIB will carry out its operations in accordance with sound management and business principles and practices. It will increase its operations in the field of development finance.
- (b) MIB will extend financial assistance only for projects which appear viable from economic, technical and financial points of view. MIB will pay special attention to the quality of the management of the enterprise and to the market prospects of the project.
- (c) MIB may assist applicants in the preparation of project applications and feasibility studies.
- (d) MIB will require eligible borrowers to finance a reasonable portion of the total project cost from their own resources to ensure that they have a reasonable stake in the projects financed by MIB.
- (e) Borrowers must not be in arrears in the repayment of either principal or interest on any existing loan.
- (f) For the projects assisted by it, MIB will ensure availability of all financial requirements, including working capital, for the successful implementation of the project.
- (g) MIB will appropriately supervise the use of its funds, the progress of the project financed and the performance of the enterprise so and to ensure that remedial action is promptly taken when problems arise. Whenever necessary, MIB will endeavour to provide the necessary technical services to such enterprises.
- (h) MIB will determine the repayment period of loans, including grace period, in accordance with the nature and the individual circumstances of the project.

IV. Financial Guidelines

- (a) MIB will finance its medium- and long-term operations from its long-term resources and it shall endeavour to diversify its investments in terms of the type of industries, the location of such industries and the type of financing.
- (b) MIB will not seek to control any of the enterprises in which it has invested nor will it participate in the management of such enterprises except for the purpose of safeguarding its interest.

- (c) In accordance with sound banking practices, MIB will secure its loans and guarantees with appropriate collateral from its client; but MIB will have due regard to its developmental functions in the Korean economy. In making investments in equity participations and in underwriting stocks and debentures of its clients, MIB will be guided by considerations of technical feasibility, financial viability and economic justification of the projects and enterprises so assisted.
- (d) MIB will not subscribe to stocks in excess of its unimpaired paid-up capital, legal reserves and surplus. As a rule, MIB's equity participation in any single enterprise shall not exceed 25% of the paid-in capital stock of an enterprise. MIB's equity investment shall serve mainly as a catalytic agent for the establishment of new enterprises and MIB will endeavour to dispose of such equity investments as soon as this becomes feasible at a fair price.
- (e) MIB's total commitments in any one single enterprise in whatever form, i.e. loans, equity participation, guarantees or a combination thereof, will normally not exceed 25% of the sum of its unimpaired paid-in capital, legal reserves and surplus.
- (f) In general, MIB's total commitments in any one single enterprise will not exceed 60% of the total assets of the enterprise including MIB's own investments. Exceptions to the above may be made in respect to MIB's financing of small and medium industry cooperatives, local governments and nonprofit seeking corporations.

V. Accounting

- (a) MIB will maintain accounting records adequate to reflect its business operations and affairs in accordance with generally accepted accounting principles and standards.
- (b) MIB will engage a qualified and independent public accountant to audit its books and financial statements every year.

VI. Provisions and Reserves

- (a) MIB will annually make appropriate allocations to a provision for the protection against bad debts and investments until such provision equals 10% of MIB's portfolio.
- (b) MIB will allocate at least 25% of its annual net profits to a reserve fund until such a reserve fund reaches a sum equal to its paid-up capital.

KOREAMEDIUM INDUSTRY BANKOutline of Development Strategy for 1978/79

In parallel with the projected expansion of its financing operations in the two-year period 1978/79, MIB will endeavour to further enhance its impact on the Small and Medium Industry (SMI) Sector through the implementation of some of the developmental objectives outlined below.

- (a) Notwithstanding the recent upward revision of the official definition of SMI enterprises eligible for MIB's financing, it is MIB's policy and intention, apart from financing medium-sized enterprises (as presently redefined), to make special efforts to seek out and assist an increasing number of small enterprises (in terms of total assets) and labor intensive projects (in terms of the labor/capital ratio). This emphasis on financing small, labor intensive projects will apply to the use by MIB of IBRD resources as well as its other resources.
- (b) As it has done since 1975, MIB will continue to gradually increase the proportion of its financing to areas outside metropolitan Seoul and Pusan. It is intended that such proportion would be below 50% for the 1978/79 period. One specific objective of this geographic dispersal is to achieve the transfer of excess manpower from rural areas to small factories located in nearby small towns.
- (c) MIB will continue to intensify its assistance to small rural industries within the Saemaul Program.
- (d) MIB will reexamine its role, methods and means for providing appropriate extension services (technical, managerial) to SMI enterprises, within the context of the general study on Korean SMI and on extension services which the Government is planning to undertake in the near future.
- (e) MIB will intensify its research activities, with particular emphasis on feasibility studies and market studies for selected SMI activities.

KOREA
MEDIUM INDUSTRY BANK

Estimated Commitment and Disbursement Schedules
Under Proposed Bank Loan /a
(in US\$ million)

	<u>Commitments</u>		<u>Disbursements</u>	
	Amount	% /b	Amount	% /b
<u>1978</u>				
2nd quarter	5.0	9.1	-	-
3rd quarter	7.0	21.8	3.2	5.8
4th quarter	10.5	40.9	5.2	15.3
End-1978	<u>22.5</u>		<u>8.4</u>	
<u>1979</u>				
1st quarter	10.5	60.0	7.4	28.7
2nd quarter	8.5	75.5	8.9	44.9
3rd quarter	6.0	86.4	7.6	58.7
4th quarter	4.0	93.6	6.3	70.2
End-1979	<u>29.0</u>		<u>30.2</u>	
<u>1980</u>				
1st quarter	2.0	97.3	4.2	77.8
2nd quarter	1.5	100.0	3.3	83.8
3rd quarter	-	-	2.6	88.5
4th quarter	-	-	2.0	92.2
End-1980	<u>3.5</u>		<u>12.1</u>	
<u>1981</u>				
1st quarter	-	-	1.6	95.1
2nd quarter	-	-	1.2	97.3
3rd quarter	-	-	0.8	98.7
4th quarter	-	-	0.5	99.6
End-1981	-	-	<u>4.1</u>	
<u>1982</u>				
1st quarter	-	-	0.2	100.0
<u>Total</u>	<u>55.0</u>		<u>55.0</u>	

/a Assuming loan effectiveness in March 1978.

/b Cumulative percentages.

KOREA

MEDIUM INDUSTRY BANK

Related Documents and Data Available in the Project File

A. General Reports and Studies on the Sector or Subsector

- A.1 National Income in Korea. The Bank of Korea. 1975.
- A.2 Report on Mining and Manufacturing Survey. Economic Planning Board. 1975.
- A.3 Financial Statements Analysis for 1975. The Bank of Korea. 1976.
- A.4 Study on the Status of Small and Medium Industries in 1975. Medium Industry Bank. 1976.
- A.5 General Status of Small Business in Korea. Korea Federation of Small Business. 1977.

B. General Reports and Studies Relating to the Project

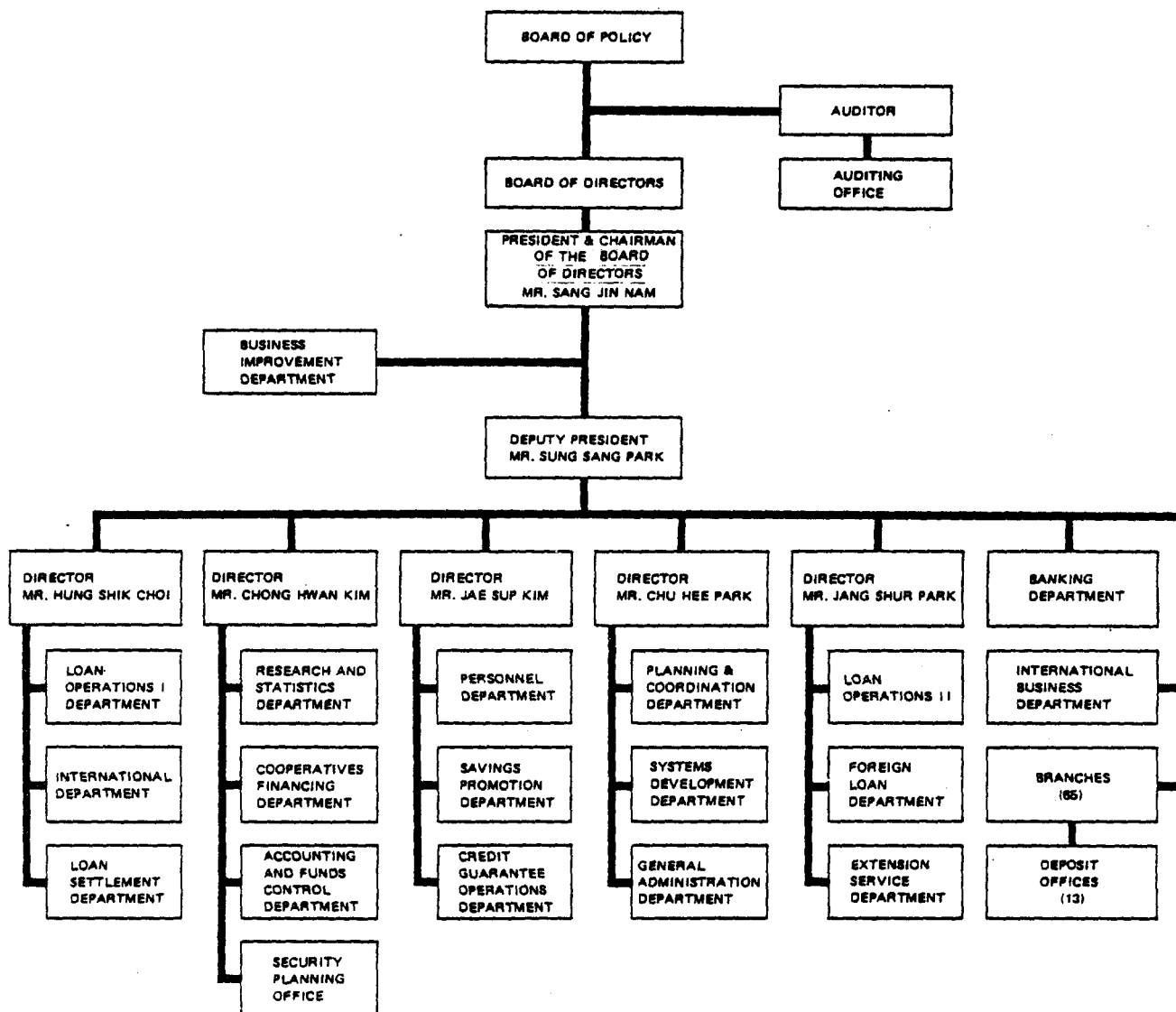
- B.1 The Medium Industry Bank Act. Law No. 641. July 1, 1961.
- B.2 Presidential Decree of August 1, 1961 as amended by Decree No. 8414 of January 18, 1977 relating to the execution of the Medium Industry Bank Act.
- B.3 Medium Industry Bank. Annual Reports 1975 and 1976.
- B.4 Medium Industry Bank. Audited Financial Statements 1974-1976.

C. Selected Working Papers

- C.1 Economic and Financial Rates of Return on a Sample of 20 MIB-Financed Subprojects.
- C.2 Foreign Exchange Component of Domestically Manufactured Machinery.

AEP Projects Department
October 28, 1977

**KOREA
MEDIUM INDUSTRY BANK**
Organization Chart as of June 30, 1977



Staffing	Head Office	Branches	Total
Professional	471	1,238	1,710
Clerical	112	443	555
Others	219	1,049	1,268
Total	802	2,731	3,533